FINANCIAL INSTITUTIONS COMMITTEE
Business Law Section, State Bar of California

Minutes of the Meeting of July 10, 2007

Committee Members Present:
Rosie Oda, Chair
Meg Troughton, Vice Chair
Bruce Belton, Secretary
Richard de la Pena
Bart Dzivi
Andrew Druch
Todd Okun
Will Stern
Shirley Thompson

Advisory Members and Others Present:
Steve Balian
Sally Brown
Ted Kitada
Bill Kroener
Mark Moore
Robert Mulford
Michael Occhiolini
Mary Price
Jim Rockett
Jason Robman
Joseph Sanchez
David Tollen
Chuck Washburn
Maureen Young

Call to Order: Rosie Oda called the meeting to order at 9:30 a.m.

1. Roll Call, Introductions and Administrative Matters: Rosie welcomed the Committee Members, Advisory Members and Guests. Rosie reported that the Bar's email listserve has had some difficulty in delivering to firms mail servers with recipient limits. Therefore in the future she will send email to the constituency list in a format where all email addresses will be listed and wanted to alert those who might have a concern about their email address being visible to others. Rosie also mentioned that elections for new members and officers will be held when Meg begins her term as Chair. Mark Moore (attending by phone) reported that he is temporarily serving as chair of the Consumer Financial Services Committee. The CFSC will be working on a project to revise California statutes addressing service of legal process on multi-branch financial institutions. The object is to draft a legislative proposal that the Bar would submit to the legislature, and to obtain consent from interested parties before the proposal is finalized. Drafts will be posted to the CFSC website. CFSC will also be looking into internet gaming issues, including the settlement of fees and charges for those services.

2. Merchant Fees Litigation. This item was deferred to the August meeting

3. Tech Contracts: David Tollen of Tollen Legal, www.tollenlegal.com (and a member of the Cyber Law Committee) made a presentation to the Committee regarding the review and negotiation of tech contracts for financial institutions. Five points were outlined to better understand technology licensing issues. David's materials are attached. This presentation is a summary of a 3 hour CLE seminar that David presents and is partly derived from his book entitled "Tech Contracts Pocket Guide" published in 2006 by iUniverse, Inc. (www.iuniverse.com).

Point one: You don't need a license to use software. Software is just text and governed by the same intellectual property law as other IP types (e.g., books, sculpture, movie etc.). No license would be needed to read a book, and likewise the right to use software is not created by a license. Instead, the license grants rights which would otherwise be exclusive to copyright holders: i.e., reproduce, modify, publicly perform, publicly display, and sublicense. Software is something that is "used" and technology providers generally view that its use is the fundamental license right. Technically, when a software license expires, the right to use the software does not (although some contracts will include a provision that requires the licensee to stop use). The point of this issue is that a license to use software renders software contracts unclear because the right to use is not exclusive to the copyright holder, and therefore must be interpreted in the context of what rights the copyright holder is actually granting to the licensee. However, scope of use rights are usually included. Just be certain that the statutory rights of the copyright holder are also included.

Point two: You gain almost nothing by owning technology (but if you do plan to own it, watch out for assignment and work-for-hire pitfalls). Software buyers often insist that because they paid for customized software programming, they should own it. Ownership grants the statutory rights discussed above to the owner. Those rights may not be of value to a business owner, other than prohibiting a competitor from using the software. Conversely, giving up the right of ownership might provide significantly greater benefits in return to the licensee. Because licensees are not in the software business perhaps little is gained by insisting on ownership. Instead the licensee needs rights to reproduce, modify, etc. The vendor may reduce the price if ownership remains with the vendor. If you are going to own the software, the law favors the person who creates the software who may have residual rights notwithstanding an assignment of the copyright (should also include a backup provision for license in case the assignment fails). Look for professional help for drafting enforceable software assignment agreements.

Point three: Most contract clauses are molehills; technical specifications are mountains. The terms and conditions may not be as important as the specifications which establish the benchmarks for software performance. Absent clear technical specifications, enforcement of warranty and indemnities will be difficult or impossible unless performance specifications are clear. Better not to delegate the entire responsibility for specifications to the vendor and client. The specifications should be readily understandable by non-tech persons, and adequate definitions for those terms that are unique to the product or hardware in use. The same review should be applied in the statement of work (or service level agreement) for a services contract.

Point four: In drafting escrow clauses, the golden rules are: (a) trust but verify; and (b) avoid the bankruptcy creditors' queue. A technology escrow provides for the deposit of source code with a third party. Source code is needed to maintain software. The purpose is to make source code available to the licensee if the vendor goes out of business. Because the buyer won't see the

code deposited in the vault until it is needed, verification should be made on deposit (i.e., compiled and run). Best to use a professional software escrow that can provide verification services. Don't enter into an escrow agreement that only gives the right to obtain and compile the source code *after* a bankruptcy is filed since the license to use the source code, if contingent on a bankruptcy filing, may result in the licensee becoming a creditor, without having obtained any present license rights to the source code. License to the source code needs to be effective on the date the contract is executed to avoid this issue. Avoid creating any rights in a license that are triggered by the filing of a bankruptcy. Also consider a backup or replacement escrow if the first one selected becomes unavailable.

Point five: You don't need a limitation of liability clause (but get one if you can). Vendor liability is usually limited, e.g., exclusion of consequential damages and inclusion of dollar damage caps. This is common in the technology industry because these companies face a unique risk because the consequences of failed software can be catastrophic. Absent limitations on liability, the costs of software could be prohibitive. For example, a relatively inexpensive software product could cause vast damages on a large scale construction project. Buyers usually ask for a limitation of liability clause as well. Vendors sometimes agree to this, but it is not critical for the buyer (and if you get one, there will usually be a number of exceptions that protect IP rights for the vendor). Perhaps it could be best to traded for something more valuable to the buyer.

4. Regulation Z Proposal. Joe Sanchez reported on the proposed updates to Regulation Z as follows: The Federal Reserve has proposed changes to Regulation Z. The primary focus is to ensure that credit card terms are disclosed in a clear and conspicuous format at the time of solicitation. Some of the proposals were based on consumer testing solicited from credit card customers. These regulations are the culmination of two previous advance notices in 2004 and 2005. The proposal also addresses consumer protection against unfair and inaccurate credit card billing practices, divided into five areas: account opening; disclosures; periodic statements; changes in terms; and advertising provisions. Rather than revise the entire regulation, the proposal is to approach this on a piecemeal basis.

The 2004 proposal received approximately 200 comments and from those the new proposal focuses on tables for disclosure and comparison purposes. Consumers liked the tables and creditors are reasonably comfortable with that approach. As credit products become more complex, the tables will be increasingly more complex, but this is arguably preferable to additional written disclosures. Other comments focused on the overwhelming information contained in current disclosure forms. Also discussed was the concept of an "effective APR" to allow for comparison which is closer to the true cost of credit (e.g., including fees and based on what an average customer paid on the account). Another proposal was to give more advance notice for change in terms; the proposal is for 45 days. Solicitation materials must also clearly and conspicuously disclose "go to" rates once the introductory rate period expires.

Consumer testing on account opening disclosures uniformly complained that they were not easily understandable. Most are never read (no surprise there). As a result there will be many more tables. Applications and solicitations will be subject to a model form with specific font sizes and layout. Default rates will be referred to as "penalty pricing." New disclosures must describe how payments are allocated, e.g., interest and non-interest bearing balances. Additional disclosures will be required to describe variable rates and provide a referral to the Federal Reserve Bank's website for further information. Foreign currency charges are moved to account opening disclosures.

Periodic statements will require that transactions be grouped by type, versus by date, and include the total dollar amount of fees and interest plus year to date charges. Open ended plans would eliminate the requirement of disclosing periodic daily rates. Published for comment was the question of whether to disclose an "effective" APR by redefining the APR to include any fees paid on the account plus interest (which is favored by consumer groups but disfavored by creditors because the disclosed rate could be very high). If a change in terms notice was to be included, then the table would be placed at the top of the statement highlighting the change in terms (a response to consumer complaints about throwing away statement stuffers). Payment posting cutoff times prior to 5pm would need to be disclosed (but this may not take into account time zone changes). An additional warning would be included indicating the time required to payoff a "generic" balance versus the actual balance by making only the minimum payment. To get the actual payoff time many assumptions would be required which may be very difficult to estimate for some creditors (e.g., variable rates).

For change in rate terms, the proposal is to expand the existing notice requirement of 15 day advance notice to 45 before implementing the new rate. The regulation may also require advance notice before imposing the penalty rate. The proposal is 30 to 45 days advance notice.

Advertising must clearly disclose how long a fixed rate lasts before expiration, and perhaps require another change in terms notice before implementing a variable or higher rate. Introductory rate disclosures must be clear and conspicuous. Credit card access checks will require additional warning disclosures. Credit or debt cancellation insurance will also require additional disclosures. The majority of the proposal consist of additional disclosures.

5. Senator Dodd's Proposed Private Student Loan Transparency and Improvement Act. Mary Price reported on a proposal, which although directed at student loans, could apply to other credit products. The proposal suggests that in pricing student loans creditors who are considering default rates are in essence "redlining" and discriminating on the basis of lower income and risk. Letters have been sent to approximately 20 student lenders asking how they are setting prices. It is suggested that companies should base the rate on the family's credit rating. Most students have no credit rating and if their parents are not on the loan then the risk is not adequately represented. A proposed bill includes an authorization for the Federal Reserve to require private lenders to collect and report data on applications aggregated by race, gender, age and type of institution. These would essentially be HMDA type disclosures for a non-real estate secured loans. This has been suggested in the past by consumer groups who have requested this type of data for quite some time. There are arguments on both sides whether it makes sense to take into account default rates for the type of school. For federal student loans, once the default rate reaches a certain level, the school would no longer be eligible for student loans.

6. IOLTA Proposal Update. Ted Kitada reported on Assembly Bill 1723 (copy attached) which represents the most significant change to IOLTAs since they were authorized in the early 1980's. The Bar has been concerned about plummeting interest rates and cutback in federal funding available to the programs funded by IOLTA and has informally approached a number of banks in California about what could be done to support the program. This issue has also been addressed in other jurisdictions in a manner similar to AB 1723. A consulting company has been advocating in other states the means by which the yields on these accounts could be increased. In some of these states, only changes to court rules were required. In others, including California, the IOLTA programs are in statute requiring legislative solutions. The State Bar took this proposal directly to the Chair of Judiciary Committee of the Assembly without consultation with the financial services industry. The proposal was then moved directly to the Legislature.

Effective next year, the financial services industry will face significant costs associated with these products.

It is expected that the June 13, 2007 version of the Bill, which included the CBA comments will pass. Staring next year those banks that don't offer investment products (e.g., mutual funds) will not need to make any changes. This will result in disparate treatment for big banks that offer investment products and money funds leaving them with two choices: (1) their investment account products must be IOLTA enabled; or (2) they can increase the rate on traditional IOLTA deposit account to achieve comparable yields to the investment accounts. Thus, for those accounts meeting minimum balance requirements, the yield must be equal to the comparable investment product account type. Fees can be offset against earnings on the accounts. Only those money funds or repo accounts that are backed by government securities are used to establish the applicable yield, and those rates are relatively low (e.g., 4%). Costs for providing these products will significantly increase. Most banks are paying under 1% and most of the yields for banks offering investment products will increase to the 4% range. If banks fail to comply, the Bar can declare those banks ineligible for IOLTAs.

7. Report on *Zengen v. Comerica Bank*. Ted also reported on the recent California Supreme Court opinion in *Zengen v. Comerica* (copy attached). A company CFO, without consent, made wire transfers totaling $4.6 million. A provision in Article 11 of the Commercial Code (4A of the UCC) contains a one year statute of limitations on such claims. The question presented to the Court was whether the company, through its officials, including the CEO had timely objected to the unauthorized wire transfers. It was clear that they were unauthorized. The Bank defended the claim on the theory that the company knew about the wires and failed to object within the one year statute. The Court ruled that Article 11 governs wire transfers in a similar fashion that Articles 3 and 4 govern negotiable instruments. But the Court reversed on the question of whether the company had objected to the wire transfers, not simply notified the Bank that the transfers were fraudulent. This materially weakened the Court of Appeal decision and enforcement of the one-year statute in Article 11.

8. OCC Letter on Bounce Check Fees. This item was deferred to the August meeting.

9. Update on State Bar Annual Meeting FIC Panel Presentation. Meg Troughton reported that the program is proceeding and expects a fine panel presentation at the Annual Meeting. She is waiting for bios and materials from the panelists who will be Meg, Sally Brown, Will Stern, Isabelle Ord, and Michael Abraham.

10. Update on BSA. This item was deferred to the August meeting.

11. Report Legislative Subcommittee. Bart Dzivi reported on House passage of the Federal Housing and Finance Reform Act which had many of the same provisions of a similar bill passed in the last session. This would create a new agency headed by one director to supervise not only FHLMC and FNMA but also the Federal Home Loan Bank. This agency will be given enhanced supervisory and regulatory powers on par with the federal banking agencies including the power to put the entities into receivership. One provision expressly allows the regulators to limit the amount of the mortgages held in portfolio by the enterprises. Language was added on the House floor that such power was based on a risk to the enterprises themselves. The Bill will establish an affordable housing fund with a five year sunset based on 1.2 basis points of the portfolios held by Fannie and Freddie and is expected to raise between $500 and $600 million per year. The first year the fund would be directed to the victims of Katrina with Louisiana getting 75% of the money and Mississippi receiving the balance. Thereafter, the Treasury

Department is to decide upon a formula allocating the funds among the 50 States and federally recognized Indian Tribes. No provision was included for the refinancing of sub-prime mortgages. Another amendment added on the House floor was to limit the Agencies' purchase of mortgages to only those where the borrower presents a valid social security number, thereby excluding foreign nationals. The loan limit in high cost metropolitan areas would be no less than 150% of the overall limit or the area median price. The current loan limit is $415,000 subject to adjustment each year. In a high cost area like San Francisco, the limit would be $625,000.

The prospects for this Bill remain uncertain. The Republicans have introduced a bill in the Senate which mirrors the House Bill. Senator Dodd's focus is on sub-prime mortgages and credit card disclosure reform.

Bob Mulford submitted his written report on pending legislation which is attached.

12. Open Meeting: Other Items of Interest.

13. Adjournment. The meeting was adjourned at 11:40. The next regular meeting will be August 14, 2007 at the usual locations.

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CHEAT-SHEET ON TECHNOLOGY LICENSES

Presented to the Financial Institutions Committee of the Business Law Section of the State Bar of California

By David W. Tollen*

Below are key rights and restrictions a buyer should consider for the license section of an IT copyright or patent license agreement. This is a cheat-sheet and not detailed enough to replace help of counsel; the information provided may not be adequate or suitable for particular deals.

Rights:

Copyright:
- Reproduce
- Distribute
- Modify / create derivative works
- Publicly perform
- Publicly display
- Use†
- Sublicense any or all of the rights above

Patent:
- Make and have made
- Use
- Offer for sale
- Sell or otherwise dispose of
- Import (into U.S.)
- Sublicense any or all of the rights above

Scope terms:
- Exclusivity: exclusive or not
- Geographic territory: worldwide or restricted (e.g., the United States)
- Industrial territory or licensed field (e.g., "the building maintenance industry")
- Duration: perpetual or limited in time
- Revocability: irrevocable or not
- Royalties: royalty-free or not
- Transferability: transferable or not
- Restrictions on buyer's use of technology (limited only by parties' imaginations)

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* David W. Tollen is the founder and principal of Tollen Legal and the author of *The Tech Contracts Pocket Guide: Software and Services for Salespeople, Contract Managers, Business Developers, and Lawyers* (iUniverse 2006; www.TechContracts.net).

† "Use" is not an exclusive right of copyright holders. Buyers should include it but not rely on it. In other words, buyers should make sure the other rights granted cover all needs.

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TECHNOLOGY LICENSING: FIVE LITTLE-KNOWN FACTS WITH BIG IMPLICATIONS

Presentation to the Financial Institutions Committee of the Business Law Section of the State Bar of California
July 10, 2007

David W. Tollen

Agenda

0) Introduction.

1) You don't need a license to use software.

2) You gain almost nothing by *owning* technology (but if you do plan to own it, watch out for assignment and work-for-hire pitfalls).

3) Most contract clauses are molehills; technical specifications are mountains.

4) In drafting escrow clauses, the golden rules are: (a) trust but verify, and (b) avoid the bankruptcy creditors' queue.

5) You don't need a limitation of liability clause (but, heck, get one if you can).

AN OUTLINE SUMMARY OF THE FRB'S PROPOSED REVISIONS TO REGULATION Z (OPEN END)

I. Background.

A. The Federal Reserve Board ("Board") has issued a proposal making substantial revisions to Regulation Z as it pertains to open-end credit ("Proposal").

B. The Proposal is the culmination of amendments to the Truth in Lending Act ("TILA") made by the Bankruptcy Abuse Prevention and Consumer Protection Act and two Advance Notice of Proposed Rulemakings issued by the Board.

C. Comments on the Proposal must be submitted no later than 120 days after the Proposal is published in the *Federal Register*.

D. Except as otherwise described, this summary outline includes only provisions the Board proposes to change in Regulation Z. This outline does not necessarily describe every proposed change to Regulation Z in the Proposal.

E. Except as otherwise described, this outline pertains only to open-end credit card plans. Some, but not necessarily all, of the provisions may apply to other types of open-end plans.

II. § 226.4 Finance Charge.

A. *Cash Advances*. Any transaction charge imposed on a cardholder by a card issuer is a finance charge, regardless of whether the issuer imposes the same, greater, or lesser charge on a withdrawal of funds from an asset account. Comment 4(a)-4.

B. *Foreign Transactions*. Any charge imposed on a credit cardholder by a card issuer for making a purchase outside the U.S. or in a foreign currency is a finance charge, regardless of whether the card issuer imposes a charge on its debit cardholders for such transactions. Comment 4(a)-4.

C. *Debt Cancellation/Suspension/Credit Insurance.*

1. Rules applicable to debt cancellation coverage being excluded from the definition of finance charge also apply to debt suspension coverage, so long as the creditor informs the consumer that the obligation to pay loan principal and interest is only suspended, and that interest will continue to accrue during the period of the suspension. § 226.4(d)(3)(iii).

2. Coverage of credit insurance or cancellation/suspension coverage in sales made throughout the life of an open-end loan would be "written in connection with" the open-end plan, meaning that, to exclude the cost of

coverage from the definition of finance charge, consumers would need to receive the same disclosures that are generally provided when coverage is sold at the outset of the plan. Comment 4(b)(7) and (8)-2, (10)-2.

3. For telephone sales, creditors could provide disclosures orally, and consumers could affirmatively request the insurance coverage orally, if the creditor maintains evidence of compliance with the requirements (such as an audio recording), and mails written information within three days of the sale. § 226.4(d)(4).

a. A creditor does not satisfy the requirement to obtain an affirmative request if the creditor uses a script with leading questions or negative consent. Comment 4(d)(4)-1.

III. § 226.5 General Disclosure Requirements.

A. *Tabular Disclosures*. The following disclosures must be provided in tabular format (§ 226.5(a)(3)) in a minimum 10-point font (Comment 5(a)(1)-3):

1. Application, solicitation, and take-one disclosures;

2. Account-opening disclosures described in § 226.6(b)(4);

3. Disclosures on checks that access a credit card account;

4. Certain change-in-terms disclosures; and

5. Disclosures required when a rate is increased due to delinquency, default, or as a penalty.

B. *Oral Disclosures*. An issuer may disclose orally charges not specifically identified in § 226.6(b)(4) (*i.e.*, those required in the account-opening tabular disclosures) prior to the consumer agreeing to pay or becoming obligated to pay for the charge. § 226.5(a)(1)(ii)(A) and (b)(1)(ii).

1. The Board anticipates that creditors will continue to identify fees in the account agreement for contract and other reasons, but is not requiring creditors to do so.

C. *Electronic Disclosures*. Disclosures may be provided electronically subject to compliance with the applicable provisions of the E-SIGN Act. Disclosures required under § 226.5a and 226.16 may be provided electronically without regard to the E-SIGN Act. § 226.5(a)(1)(iii).

D. *Terminology*.

1. *Grace Period*.

a. Currently, disclosures required for applications and solicitations under § 226.5a must use the term "grace period" to describe the date by which or the period within which any credit extended for purchases may be repaid without incurring a finance charge.

b. This requirement is extended to all references to such a term for any tabular disclosure. § 226.5(a)(2)(iii).

2. *Penalty APR.* For disclosures required to be presented in a tabular format, the term "penalty APR" must be used to describe an increased rate that may result because of the occurrence of one or more specific events specified in the account agreement. § 226.5(a)(2)(iii).

3. *"Fixed" APR*. If required to be disclosed in a tabular format, APRs may be described as "fixed" or any similar term only if that rate will remain in effect unconditionally until the expiration of a specified time period or, if no time period is specified, the rate remains in effect unconditionally until the plan is closed. § 226.5(a)(2)(iii).

E. *No Need for More Conspicuous Disclosure of "Finance Charge" and "Annual Percentage Rate"*. These terms need not be more conspicuous than other terms when such terms are included in tabular disclosures. § 226.5(a)(2)(ii).

F. *Timing of Account-Opening Disclosures in Connection with Balance Transfer Offers.* If an issuer offers balance transfers for which the APRs that may apply are disclosed as a range, the issuer must provide the disclosures required by § 226.6 sufficiently in advance of the transfer to allow the consumer to respond to the terms that will apply to the transfer, including to contact the issuer before the balance is transferred and decline the transfer. Comment 5(b)(1)(i)-5.

G. *Timing of Account-Opening Disclosures in Connection with Telephone Purchases*. Disclosures required by § 226.6 may be provided as soon as reasonably practicable after the first transaction on an open-end plan if:

1. The first transaction occurs when a consumer contacts a merchant by telephone to purchase goods and at the same time the consumer accepts an offer to finance the purchase by establishing an open-end plan *with the merchant*;

2. The merchant permits consumers to return any goods financed under the plan and provides consumers with a sufficient time to reject the plan and return the goods free of cost after receiving the written disclosures required by § 226.6; and

3. The consumer's right to reject the plan and return the goods is disclosed to the consumer as a part of the offer to finance the purchase. § 226.5(b)(1)(iii).

H. *Timeframe for Mailing Periodic Statements.* If an issuer provides a grace period, Section 163(a) of TILA requires creditors to send periodic statements at least 14 days before the grace period ends. The Board requests comment on whether it should recommend to Congress that the 14-day period be increased and, if so, what time period the Board should recommend.

IV. § 226.5a Credit and Charge Card Applications and Solicitations.

A. *Combining Disclosures*. A card issuer may satisfy § 226.5a by providing the tabular account-opening summary described in Section V.E below on or with a card application or solicitation in lieu of the Schumer Box. Comment 5a-2.

B. *Clarification of "Solicitation."*

1. *Firm Offers of Credit.* The Proposal clarifies that "firm offers of credit" as defined by the Fair Credit Reporting Act are "solicitations" for purposes of Regulation Z. § 226.5a(a)(1).

2. *Invitations to Apply*. When an issuer contacts a consumer who has not been pre-approved for a card account about opening an account and invites the consumer to complete an application, but the contact itself does not include an application, the contact is not a "solicitation" for purposes of Regulation Z. Comment 5a(a)(1)-1.

C. *Delivery of Application and Solicitation Disclosures Electronically.*

1. If the application or solicitation is accessed by the consumer in electronic form, the disclosures required by § 226.5a must be provided in electronic form on or with the application or solicitation. § 226.5a(2)(v).

2. Applications and solicitations that are provided electronically must contain the same disclosures as applications and solicitations sent by direct mail. § 226.5a(c).

3. If the Schumer Box is provided electronically with an application or solicitation, it must be provided in close proximity to the application or solicitation. § 226.5a(2)(vi)(B).

4. Electronic disclosures would be deemed to be "closely proximate" to an application or solicitation if:

a. They automatically appear on the screen with the application or reply form;

b. They are located on the same web "page" as the application or reply form without necessarily appearing on the initial screen, if the application or reply form contains a clear and conspicuous reference to the location of the disclosures and indicates that the disclosures contain rate, fee, and other cost information, as applicable; or

c. They are posted on a web site and the application or solicitation reply form is linked to the disclosures in a manner that prevents the consumer from by-passing the disclosures before submitting the application or reply form. Comment 5a(a)(2)-1(ii).

5. The interpretive commentary regarding "closely proximate" disclosures is consistent with the commentary pertaining to the timing of disclosures for electronic applications or solicitations, which is also found in the Board's E-SIGN proposal. Comment 5a(a)(2)-8.

D. *Revisions to Schumer Box.*

1. *Grouping of Disclosures.* A issuer must group disclosures of interest rates together and group disclosures of fees together. Appendix G-10(A)-(C).

2. *Fees for Late Payment, Over-Limit, Balance Transfers, and Cash Advances.* Current law provides that an issuer may disclose such fees in the table or outside the table. The Proposal would require such fees to be disclosed in the table. § 226.5a(a)(2)(i).

3. *Rates and Fees in Bold in Table*. An issuer must disclose in bold text any APRs required to be disclosed, any discounted initial rate permitted to be disclosed, and any fee amounts or percentages required to be disclosed, except for any maximum limits on fee amounts disclosed in the table. § 226.5a(a)(2)(iv).

4. *Font Size of Purchase APR.* The current 18-point font requirement for the purchase APR is 16-point under the Proposal. § 226.5a(b)(1).

5. *No Periodic Rate*. Issuers may not disclose the periodic rate in the table. Deletion of Comment 5a(b)(1)-1.

6. *No Disclosure of Variable Rate Index or Margin*.

a. In connection with a variable rate, an issuer may not disclose the index or margin in the table.

b. An issuer may indicate only that the rate varies and the type of index used to determine the rate, such as "prime rate". § 226.5a(b)(1)(i) and Comment 5a(b)(1)-2.

7. *No Disclosure of Rate Floors or Ceilings.* An issuer may not disclose a rate floor or ceiling in the table. Deletion of Comment 5a(b)(1)-4.

8. *Introductory Rates.* If the issuer discloses an introductory rate in the table, the issuer must use the term "introductory" or "intro" in immediate proximity to the listing of the initial discounted rate. § 226.5a(b)(1)(ii).

a. Placing "introductory" or "intro" "within the same phrase" as the introductory rate would be a safe harbor. Comment 5a(b)(1)-3.

9. *Penalty Rates.*

a. An issuer must disclose, briefly, the specific event or events that may result in a penalty rate in the same row of the table.

b. An issuer must also specify the balances to which the increased rate will apply, and the duration of the increased rate.

c. In disclosing a penalty rate, an issuer must include a brief description of the circumstances under which any discounted initial rates may be revoked and the rate that will apply after the discounted rate is revoked. § 226.5a(b)(1)(iv) and Comment 5a(b)(1)-4.

10. *Rates Based on Risk-Based Pricing.* In circumstances in which an issuer cannot state a single specific rate being offered at the time disclosures are given because the rate will depend on a later determination of the consumer's creditworthiness, the issuer must disclose the possible rates that might apply and a statement that the rate for which the consumer may qualify at account opening depends on the consumer's creditworthiness.

a. The issuer could disclose the possible rates either as specific rates or a range of rates. § 226.5a(b)(1)(v) and Comment 5a(b)(1)-5.

11. *Cross References Between Rates and Fees.*

a. If a rate and a fee both apply to a balance transfer or cash advance transaction, the issuer must disclose that a fee also applies when disclosing the rate, and provide a cross-reference to the fee. § 226.5a(b)(1)(vi).

b. If an issuer may impose a penalty rate for any of the reasons that a

penalty fee would be disclosed in the table, the issuer in disclosing the fee must also disclose that the penalty rate may apply, and provide a cross-reference to the rate. § 226.5a(b)(13).

12. *Fees for Issuance or Availability.*

a. Currently an issuer must disclose only the annualized amount of a periodic fee. The Proposal would require an issuer to disclose the amount of the periodic fee and how frequently it will be imposed. § 226.5a(b)(2)(i).

b. Currently an issuer must disclose the amount of a non-periodic fee, but not that it is a one-time fee. The Proposal would require an issuer to disclose the amount of the fee and that it is a one-time fee. § 226.5a(b)(2)(ii).

c. An issuer must disclose application fees in the table. Revision of Comment 5a(b)(2)-3 and § 226.4(c)(1).

13. *Foreign Currency/Transaction Fees.* An issuer may not disclose fees for transactions in a foreign currency or that take place in a foreign country in the table. § 226.5a(b)(4)(ii).

14. *Grace Period.* An issuer must disclose briefly any conditions on the applicability of the grace period. § 226.5a(b)(5) and Comment 5a(b)(5)-1.

15. *Balance Computation*. An issuer must make a brief reference to the balance computation method, but move the disclosure from the table to directly below the table. § 226.5a(a)(2)(iii) and (b)(6).

16. *Returned Payment Fee*. An issuer must disclose returned payment fees in the table. § 226.5a(b)(12).

17. *Required Insurance, Debt Cancellation, or Debt Suspension Coverage.* If an issuer requires insurance or debt cancellation/suspension coverage (to the extent permitted by applicable law), the issuer must disclose any fee for this coverage in the table. § 226.5a(b)(14).

18. *Payment Allocation*. If a card issuer (i) offers a discounted initial rate on a balance transfer or cash advance that is lower than the rate on purchases; (ii) offers a grace period on purchases; and (iii) may allocate payments to the lower rate balance first, the issuer must disclose that:

a. The discounted initial rate applies only to balance transfers or cash advances (as applicable) and not to purchases;

b. Payments will be allocated to the balance transfer or cash advance balance before being allocated to any purchase balance during the time the discounted initial rate is in effect; and

c. The consumer will incur interest on the purchase balance until the entire balance is paid, including the transferred balance or cash advance balance. § 226.5a(b)(15).

d. The required disclosures apply only to balance transfers or cash advances that consumers can request as part of accepting the offer.

19. *Available Credit.* If an issuer imposes required fees for the issuance or availability of credit, or a security deposit, that will be charged against the card when the account is opened, and the total of those fees equals 25% or more of the minimum credit limit applicable to the card, the issuer must disclose in the table an example of the amount of the available credit that a consumer would have remaining after these fees are debited to the account, assuming the consumer receives the minimum credit limit offered. § 226.5a(b)(16).

20. *Reference to Board Web Site.* An issuer must disclose in the table a reference to a Board web site and a statement that consumers can find on the site educational materials on shopping for and using credit card accounts. § 226.5a(b)(17).

21. *Telephone Disclosures*. Currently, an issuer is not required to provide certain cost disclosures if the issuer does not impose a fee for the issuance of the card or does not impose such a fee unless the consumer uses the card, provided that the issuer provides the Schumer Box in writing within 30 days of the request (but no later than the delivery of the card). The Proposal would allow an issuer to disclose in the table that the consumer is not required to accept the card or pay any fee unless the consumer uses the card. Comment 5a(d)-2.

E. *Take-One Applications and Solicitations.*

1. An issuer that provides cost disclosures in take-one applications and solicitations must provide the Schumer Box disclosures. § 226.5a(e)(1) and Comment 5a(e)-1.

2. The option to provide a narrative that describes how finance charges and other charges are assessed is no longer available.

3. The required disclosures must be accurate as of the date of printing, although the variable APR may be accurate within 30 days of printing. § 226.5a(e)(4).

F. *In-Person Applications and Solicitations.*

1. An in-person application or solicitation is one initiated by the card issuer, and can include solicitations made by a retailer, or applications submitted in response to an invitation, to apply for "the retailer's credit card" at the point of sale.

2. An issuer must provide the Schumer Box for in-person solicitations or applications.

3. The Schumer Box must be accurate as of the date given (consistent with direct mail rules) *or* when printed (consistent with one option for take-one applications or solicitations). § 226.5a(f).

G. *Paper Size for Schumer Box.* The Board envisions, but does not require, the Schumer Box to be provided on 8"x14" paper. Appendix G.

H. *Accuracy of Variable Rates in Electronic Disclosures.* Variable rates disclosed on applications and solicitations provided in electronic form must be accurate as of 30 days from the date they are sent via e-mail or viewed on a web site. § 226.5a(c)(2)(ii).

V. § 226.6 Account-Opening Disclosures.

A. *Content*. The account-opening disclosures must disclose:

1. "Charges imposed as part of an open-end (not home-secured) plan" (§ 226.6(b)(1));

2. Items relating to rates for open end plans, similar to the current requirements pertaining to the circumstances under which a finance charge will be imposed and an explanation of how it will be imposed (§ 226.6(b)(2)(i));

3. Items relating to variable-rate accounts (§ 226.6(b)(2)(ii));

4. Items relating to rate changes included in the account agreement (§ 226.6(b)(2)(iii));

5. Items relating to optional credit insurance, debt cancellation, or debt suspension (§ 226.6(b)(3));

6. The account-opening tabular disclosure (§ 226.6(b)(4)); and

7. Security interest and billing rights disclosures similar to those currently

required (§ 226.6(c)(1) and (2)).

B. *Charges Imposed as Part of the Plan*. The Board has provided an exhaustive list of charges that are imposed as part of the plan. They are:

1. Finance charges identified under § 226.4(a) and (b);

2. Charges resulting from the consumer's failure to use the plan as agreed except amounts payable for certain post-default activities;

3. Taxes imposed on the credit transaction;

4. Charges for which the payment, or nonpayment, affect the consumer's access to the plan, the duration of the plan, the amount of credit extended, the period for which credit is extended, or the timing or method of billing or payment;

5. Charges imposed for terminating a plan; and

6. Charges for voluntary credit insurance, debt cancellation, or debt suspension. § 226.6(b)(1)(i).

7. *Some Ambiguity Remains.*

a. The description of charges in Section V.B.4. directly above is intended to be broad.

b. The Board provides guidance as to what charges are covered, such as application fees, fees to expedite card delivery, and fees to expedite payment. Comment 6(b)(1)(i)-2.

C. *Variable Rate Disclosures.* For accounts with interest rate changes that are specifically set forth in the account agreement and are tied to increases in an index or formula, the issuer must disclose:

1. The fact that the APR may increase;

2. How the rate is determined, including the margin;

3. The circumstances under which the rate may increase;

4. The frequency with which the rate may increase;

5. Any limitation on the amount the rate may change; and

6. The effect(s) of an increase. Comment 6(b)(2)(ii).

7. A rate is accurate if it is a rate as of a specified date within 30 days of the disclosures being provided.

D. *Interest Rate Changes Set Forth in Agreement, But Not Tied to an Index.* For accounts with interest rate changes that are specifically set forth in the account agreement but not tied to an index or formula, the issuer must disclose:

1. The initial rate as both a periodic rate and APR;

2. How long the initial rate will remain in effect or the specific events that cause the initial rate to change;

3. The rate (as both a periodic rate and APR) that will apply when the initial rate is no longer in effect and any limitation on the time period the new rate will remain in effect; and

4. Whether the new rate will apply to balances outstanding at the time of the change.

E. *Tabular Disclosures.* Certain information must be disclosed in the form of a table, in which no other information may appear. The information required in the account-opening table is described below. § 226.6(b)(4).

1. *APRs.*

a. An issuer must disclose each periodic rate (expressed as an APR) that may be used to compute the finance charge on an outstanding balance for purchases, cash advances, or balance transfers.

b. The APR for purchases must be in at least 16-point type except for a temporary promotional rate or a penalty rate.

c. If the rate is variable, the issuer must disclose that fact and how the rate is determined. The value of the index and the amount of the margin may not be included in the table.

d. If an initial rate is temporary, the issuer must disclose the initial rate, the circumstances under which it expires, and the subsequent rate.

e. If an initial rate is temporary and lower than the "go to" rate, an issuer must disclose the circumstances under which the promotional rate may be revoked and the rate that will apply.

f. If there is a penalty rate, the issuer must disclose the types of balances to which the penalty rate will apply, a brief description of the penalty event(s), and a brief description of how long the increased rate will remain in effect.

g. If both a rate and a fee apply to a balance transfer or a cash advance, the issuer must disclose that a fee also applies when disclosing the rate and provide a cross reference to the fee.

2. *Fees.* An issuer must disclose:

a. Any annual or periodic fee that may be imposed for the issuance or availability of an open-end plan. The issuer must disclose the amount of the periodic fee, how frequently it will be imposed, and the annualized amount of the fee.

b. Any non-periodic fee that relates to the opening of the plan, and the fact that it is a one-time fee.

c. Any transaction charge imposed on purchases, for cash advances, or to transfer balances, including ATM fees or foreign currency/transaction fees.

d. Any fee imposed for a late payment, exceeding a credit limit, or for a returned payment.

e. If an issuer may impose a penalty rate in connection with a late payment, over-limit, or returned payment fee, the issuer must also disclose that the penalty rate also apply and a cross reference to the fee [the Proposal should probably require a cross reference to the *rate*, not the fee].

f. Any minimum or fixed finance charge that could be imposed during a billing cycle and a brief description of the charge.

3. *Grace Period.* The issuer must explain whether or not a grace period applies.

4. *Required Insurance, Debt Cancellation, or Debt Suspension Coverage.* The issuer must disclose the fee for coverage if it is required as part of the plan and provide a cross reference to any additional information provided about the coverage.

5. *Payment Allocation.* If the issuer offers a discounted initial rate on a balance transfer or cash advance that is lower than the rate on purchases, and the issuer offers a grace period on purchases, and the issuer allocates

payments to the lower rate balance first, the issuer must disclose that payments will be allocated to the lower rate balance first and that the consumer will incur interest on the higher rate balance until the lower rate balance is paid.

6. *Available Credit.* If the issuer requires fees for the issuance or availability of an open-end plan, or a security deposit, and the total amount of those fees when the account is opened and charged to the account equals 25% or more of the minimum credit limit offered, the issuer must disclose the amount of the available credit that a consumer will have remaining after the fees are charged, assuming the consumer receives the minimum credit limit.

7. *Board Web Site.* An issuer must provide a reference to the Board's web site and a statement that consumers may obtain information from the site about shopping for and using credit card accounts.

8. *Balance Computation*. The issuer must disclose the name of the balance computation method that is used to determine the balance for purchases on which the finance charge is computed and a statement that an explanation of the method is provided with the account-opening disclosures.

9. *Billing Errors*. The issuer must include a statement that information about a consumer's right to dispute transactions is included in the account-opening disclosures.

F. *Paper Size for Account-Opening Table.* The Board envisions, but does not require, the account-opening table to be provided on 8"x14" paper. Comment-5(v), Appendix G.

G. *Timing*.

1. Certain charges described in 226.6(b)(4) must be disclosed in writing at account opening, or before they are increased or newly introduced. § 226.5(b)(1) and § 226.9(c)(2).

2. Any fees not described in 226.6(b)(4) are not required to be disclosed in writing at account opening. They may be disclosed orally at any relevant time before the consumer agrees to or becomes obligated to pay the charge. § 226.5(b)(1)(ii).

VI. § 226.7 Periodic Disclosures.

A. *Identification of Transactions*. The Proposal retains the current requirement to identify each credit transaction per § 226.8, but requires each transaction to be grouped by type of transaction in a form substantially similar to Sample G-18(A).

§ 226.7(b)(2).

B. *Credits*. The Proposal retains the current requirements pertaining to account credits, but such credits must be grouped together, and grouped with transactions identified on the periodic statement, in a form substantially similar to Sample G-18(A). § 226.7(b)(3).

C. *Periodic Rates*.

1. The Proposal eliminates the requirement to disclose periodic rates on periodic statements.

2. Issuers must label the annual percentage rate disclosed as "annual percentage rate." § 226.7(b)(4)(i).

3. Issuers must disclose promotional rates on the periodic statement only if the rate actually applied during the billing period. § 226.7(b)(4)(ii).

D. *Balance on which Finance Charge Is Computed.*

1. An issuer is permitted to not include an explanation of how the finance charge may be verified for issuers that use a daily balance method. The issuer may identify the name of the balance computation method and provide a toll-free telephone number where consumers can obtain more information about the computation method and how finance charges were determined. § 226.7(b)(5).

2. The issuer must disclose the amount of the balance to which a periodic rate was applied and an explanation of how that balance was determined using the term "balance subject to interest rate." § 226.7(b)(5).

E. *Charges Imposed*.

1. *In General.* An issuer must disclose the amount of any charge imposed as part of an open-end plan, grouped together, in proximity to transactions identified. § 226.7(b)(6)(i).

2. *Interest Charges.*

a. An issuer must disclose finance charges attributable to periodic interest rates, using the term "interest charge."

b. Such charges must be grouped together under the heading "interest charged," itemized and totaled by type of transaction.

c. An issuer must also disclose a total interest charge, using the term "total interest charge," for the statement period and calendar year to date. § 226.7(b)(6)(ii).

3. *Fees.*

a. An issuer must disclose any charge imposed as part of the plan other than interest.

b. Such charges must be grouped together under the heading "fees," identified consistent with the feature or type, and itemized.

c. An issuer must disclose a total of charges, using the term "fees," for the statement period and the calendar year to date.

d. An issuer must label certain fees as a "transaction fee" or a "fixed fee." § 226.7(b)(6)(iii).

F. *Effective Annual Percentage Rate.* The Proposal includes two approaches with respect to the effective APR. One approach would eliminate the requirement to disclose the effective APR. The other approach is described below.

1. An issuer must label the effective APR as the "fee-inclusive APR" and indicate that the fee-inclusive APRs are the "APRs that you paid this period when transactions or fixed fees are taken into account as well as interest." § 226.7(b)(7)(i).

2. An issuer must disclose an effective APR for each feature, such as purchases, cash advances, and balance transfers, in a tabular format. A composite effective APR for two or more features would no longer be permitted.

3. The effective APR would appear in a table, by feature, with the total interest ("interest charges") and the total of the fees included in the effective APR ("transaction and fixed charges").

4. A specific and exclusive list of finances charges used to calculate the effective APR is included in § 226.14(e).

5. The Proposal appears to suggest that if the only finance charges in a billing cycle are interest charges, the effective APR disclosures are not required. § 226.7(b)(7)(i).

G. *Due Date and Late Payment Costs*. An issuer must disclose:

1. The due date for payment, if a late payment fee or penalty rate may be imposed.

a. The Board interprets this to be a date that is required by the legal obligation and not to encompass informal "courtesy periods." Comment 7(b)(11)-1.

2. A cut-off time, if the issuer imposes a cut-off time before 5 p.m. for payment to be received.

a. If the cut-off time differs depending on method of payment, the issuer must state the earliest time if before 5 p.m. without specifying the payment method to which it applies.

3. The amount of the fee and any increased APRs that may be imposed as a result of the late payment. § 226.7(b)(11).

a. If a range of fees may be assessed, the issuer must disclose the highest fee.

b. If the APR may be increased for more than one feature or balance, the creditor must state the highest rate that could apply.

H. *Minimum Payment Disclosures.* An issuer may have to make minimum payment disclosures, described in Section VII below. § 226.7(b)(12).

I. *Change-In-Terms and Penalty Rate Summaries*. An issuer may have to make change-in-terms or increased penalty rate disclosures, described in Section IX below.

J. *Format Requirements.*

1. The issuer must disclose the due date on the front of the first page of the statement.

2. The issuer must disclose the cut-off time, the amount of the late fee, and the penalty APRs "in close proximity" to the due date.

3. The issuer must disclose the ending balance and the minimum payment disclosure "closely proximate" to the minimum payment due.

4. The issuer must group together due date, cut-off time, late fee, penalty APR, ending balance, minimum payment due, and minimum payment disclosure in a manner substantially similar to Samples G-18(E) or G-18(F). § 226.7(b)(13).

5. The format requirements for change-in-terms and penalty rate disclosures are described in Section IX below.

K. *Model Forms*. For the first time, the Board is proposing model forms designed to comply with the requirements of § 226.7. Forms G-18(G) and G-18(H).

VII. § 226.7(b)(12) Minimum Payment Disclosures.

A. *Actual Repayment Period*. An issuer has the option to provide one of two periodic statement disclosures pertaining to actual repayment periods. An issuer that provides such disclosures need not provide the disclosures described in Section VII.B. immediately below. The Board strongly encourages issuers to provide the actual repayment period disclosures and solicits comments on whether the Board can take additional steps to provide incentives to issuers to do so.

1. *Toll-Free Number to Obtain Estimate*. A creditor may:

a. Disclose on the periodic statement: "**Notice About Minimum Payments**: If you make only the minimum payment each period, you will pay more in interest and it will take you longer to pay off your balance. For more information, call this toll-free number: _____."; and

b. Establish and maintain a toll-free number for the purpose of providing consumers with the actual repayment period disclosure.

2. *Estimate on Statement*. A creditor may provide on the periodic statement a disclosure of the actual repayment information. § 226.7(b)(12)(ii).

3. *Guidance on Calculating Actual Repayment Periods*. The Board would require calculations to be based on the minimum payment formula, the APRs, and the balance applicable to the consumer's account. The Board would allow for certain assumptions with respect to balance computation, grace periods, residual interest, and payment allocation. Appendix M-2.

B. *Generic Disclosures.* An issuer that does not provide the actual repayment estimate must provide the generic minimum payment disclosure. If the issuer is a bank and has a minimum payment of less than 4% of the balance on which finance charges accrue, the issuer must:

1. Disclose on the periodic statement: "**Notice About Minimum Payments**: If you make only the minimum payment each period, you will pay more in interest and it will take you longer to pay off your balance. For example, if you had a balance of $1,000 at an interest rate of 17% and always paid only the minimum required, it would take over 7 years to repay this balance. For an estimate of the time it would take to repay your actual

balance making only minimum payments, call: _____."; and

2. Maintain a toll-free telephone number to provide generic repayment estimates. (For the first two years, certain small banks may provide a toll-free telephone number operated by or on behalf of the Board.) § 226.7(b)(12)(i).

C. *Exceptions*. The minimum payment disclosures are not required for, among other things:

1. Credit card accounts where a fixed repayment period for the account is disclosed in the account agreement and the required minimum payments will amortize the outstanding balance within the fixed repayment period; or

2. A billing cycle where a consumer has paid the entire balance in full for that billing cycle and the previous billing cycle, or had a zero outstanding balance or credit balance in those two billing cycles. § 226.7(b)(12)(iii).

D. *Toll-Free Numbers.*

1. In responding to a request for generic repayment estimates or actual repayment disclosures through a toll-free number, an issuer may not provide any information other than the repayment information required or permitted. § 226.7(b)(12)(iv).

2. If a consumer requests the repayment information, an issuer may not provide advertisements or marketing materials to the consumer prior to providing the information required or permitted. Comment 7(b)(12)(iv)-3.

3. An issuer may use a telephone number that connects consumers to an automated system. Consumers whose telephones are not equipped to use such a system must be provided the opportunity to connect to an individual from whom the information may be obtained. Comment 7(b)(12)(iv)-2.

VIII. § 226.9 Subsequent Disclosure Requirements.

A. *Billing Rights*. The requirements with respect to billing rights disclosures are unchanged, although the Board has revised Model Forms G-3 and G-4 to improve the readability of the billing rights notices.

B. *Supplemental Devices*. The Board is retaining the disclosure requirements applicable to supplemental credit devices or features, but adding requirements pertaining to convenience checks.

C. *Convenience Checks.* Convenience checks provided more than 30 days after account-opening disclosures, or those that have finance charge terms that differ from the disclosures previously given, must have certain disclosures "on the front of the page containing the checks" in the form of a table.

1. *Temporary Discount APR.* If there is a temporary discount APR, the issuer must disclose the discounted initial rate and the time period during which such rate is effective. The issuer must use the word "introductory" or "intro" in immediate proximity to the listing of the discounted initial rate.

2. *APRs Generally*.

a. The issuer must disclose the type of rate that will apply to the checks, such as purchase or cash advance, and the applicable APR.

b. If there is an introductory discount APR, the issuer must disclose the type of rate that will apply after its expiration and the APR that will apply.

c. For a variable rate account, the issuer must disclose an APR based on the applicable index or formula.

3. *Transaction Fees*. The issuer must disclose any transaction fees applicable to the convenience checks.

4. *Grace Period*. The issuer must disclose whether or not a grace period is given with credit extended through use of the checks. If no grace period is given, the issuer must state that no grace period applies and interest will be charged immediately. § 226.9(b)(3)(i).

5. *Accuracy*. The convenience check disclosures must be accurate as of the time they are given. A variable APR is accurate if it was in effect within 30 days of when disclosures were given. § 226.9(b)(3)(ii).

IX. § 226.9(c) Change in Terms/Penalty Pricing Disclosures.

A. *Change In Terms*.

1. *45-Day Notice.* For most terms required to be disclosed under § 226.6, if an issuer changes such terms, or increases the required minimum monthly payment, the issuer must provide a written notice of the change at least 45 days prior to the effective date of the change to each consumer who may be affected. § 226.9(c)(2)(i).

2. *45-Day Period Not Always Required.* If the changed term is generally not one included in the account-opening table, the issuer may provide written or oral notice of the amount of the charge at a relevant time before the consumer agrees to or becomes obligated to pay the charge. § 226.9(c)(2)(ii).

3. *Disclosure Requirements*. If the issuer changes a term disclosed in the account-opening table, the issuer must provide the following information:

a. A summary of the changes made to the term(s) in a tabular format substantially similar to any found in G-17;

b. A statement that changes are being made to the account;

c. A statement indicating the consumer has the right to opt out of these changes, if applicable, and a reference to additional information describing the opt-out right provided in the notice, if applicable;

d. The date the changes will become effective;

e. If applicable, a statement that the consumer may find additional information about the summarized changes, and other changes to the account, in the notice; and

f. If the creditor is changing a rate on the account, other than a penalty rate, a statement that if a penalty rate currently applies to the consumer's account, the new rate described in the notice will not apply to the consumer's account until the consumer's account balances are no longer subject to the penalty rate. § 226.9(c)(2)(iii).

4. *Disclosures as Part of Periodic Statements*. If the change-in-terms notice is provided on or with a periodic statement, the issuer must disclose the tabular summary of changes made on the periodic statement beginning on the front of the first page of the periodic statement directly above the groupings of transactions, credits, fees, and interest.

a. The disclosure may continue on the front of the second page if necessary, so long as there is a reference on the first page indicating the information continues on the following page.

b. The table must immediately follow the other information required to be disclosed in a format substantially similar to Sample G-20. § 226.9(c)(2)(iii)(B)(2).

5. *Disclosures Separate from Periodic Statement.* If the change-in-terms notice is not included on or with a periodic statement, the issuer may

disclose the summary table on the front of the first page of the notice or segregated on a separate page from other information given with the notice.

a. The table may be on more than one page, and may use both the front and reverse sides, so long as the table begins on the front of the first page of the notice and there is a reference on the first page indicating that the table continues on the following page.

b. The table must immediately follow the other information required to be disclosed in a format substantially similar to Sample G-20. § 226.9(c)(2)(iii)(B)(3).

6. *Notice Not Required*. Change-in-terms notices are not required when the change involves charges for documentary evidence, a reduction of any component of a finance or other charge, suspension of future credit privileges or termination of an account or plan, or when the change results from an agreement involving a court proceeding. § 226.9(c)(2)(iv).

7. *Reduction of Credit Limit*. If an issuer decreases the credit limit on an account, advance notice of the decrease must be provided before an over-limit fee or a penalty rate can be imposed solely as a result of the consumer exceeding the newly decreased credit limit.

a. The issuer must provide notice in writing or orally at least 45 days prior to imposing the fee or penalty rate and must state that the credit limit on the account has been or will be decreased. § 226.9(c)(2)(v).

B. *Penalty Rates*. An issuer must provide a written notice to each consumer who may be affected when a rate is increased due to the consumer's delinquency or default or a rate is increased as a penalty for one or more events specified in the account agreement, such as making a late payment or obtaining an extension of credit that exceeds the credit limit. § 226.9(g)(1).

1. *Timing*.

a. An issuer must provide the written penalty rate notice at least 45 days prior to the effective date of the increase.

b. An issuer must provide the written penalty rate notice after the occurrence of the penalty triggering events.

2. *Disclosure Requirements.* The issuer must provide the following information as part of a penalty rate notice:

a. A statement that the consumer's actions have triggered the

delinquency or default rate or penalty rate, as applicable;

b. The date on which the delinquency or default rate or penalty rate will apply;

c. The circumstances under which the delinquency or default rate or penalty rate, as applicable, will cease to apply, or that the rate will remain in effect for a potentially indefinite period of time; and

d. A statement indicating to which balances the delinquency or default rate or penalty rate will be applied, as applicable. § 226.9(g)(3)(i).

3. *Notice with Periodic Statement*. If the penalty rate notice is included on or with a periodic statement, the required information must be in the form of a table and provided on the front of the first page of the periodic statement directly above the grouping of transactions, credits, fees, and interest, or above a change-in-terms notice if one is included. § 226.9(g)(3)(ii)(A).

4. *Notice not with Periodic Statement*. If the penalty rate notice is not included on or with a periodic statement, the required information must be disclosed on the front of the first page of the notice. Only information related to the increase in the rate may be included with the notice, except that the notice may be combined with a change-in-terms notice. § 226.9(g)(3)(ii)(B).

X. § 226.11(b) Account Termination.

A. *In General*. An issuer may not terminate an account prior to its expiration date solely because the consumer does not incur a finance charge. § 226.11(b)(1).

1. The credit agreement determines whether or not an open-end plan has a stated expiration date. Comment 11(b)-1.

B. *Inactivity*. Nothing in § 226.11(b)(1) prohibits a creditor from terminating an account that is inactive for three consecutive months.

1. An account has been inactive if no credit has been extended and if the account has no outstanding balance. § 226.11(b)(2).

XI. § 226.12 Special Credit Card Provisions.

A. *Unauthorized Use*. The Board clarifies that if a cardholder furnishes a credit card to another person, and that person exceeds the authority given, the cardholder is liable for the transaction unless the cardholder has notified the issuer that use of the card by that person is no longer authorized. Comment 12(b)(1)(ii)-3.

XII. § 226.13 Billing Error Provisions.

A. *Use of Third-Party Intermediary*. Currently, the term "billing error" includes disputes about property or services that are not accepted by the consumer or not delivered to the consumer as agreed. The Proposal "clarifies" that when an extension of credit from the consumer's credit card is used to fund a purchase through a third-party payment intermediary (*e.g.*, PayPal), the good or service purchased is not the payment medium, but rather the good or service that is obtained using the payment service. Comment 13(a)(3)-2.

B. *Billing Error Notice*. Billing error notices submitted electronically would be deemed to satisfy the requirement that such notices be provided in writing if the issuer has stated in the billing rights statement that it will accept notices electronically. Comment 13(b)-2.

C. *Rules Pending Resolution*. If the cardholder has enrolled in the issuer's automatic payment plan, the issuer may not deduct any part of a disputed amount or related charges in connection with such an automatic payment. § 226.13(d)(1) and Comment 13(d)(1)-4.

XIII. § 226.14 Determination of APR.

A. *In General*. The Proposal does not make significant modifications to provisions dealing with tolerances for the APR and guidance on calculating the APR for certain disclosures other than the periodic statement.

B. *Two Alternatives*. The Board is proposing two alternatives with respect to the effective APR, consistent with the alternatives provided pertaining to periodic statements.

1. The first alternative revises the calculations for the effective APR.

2. The second alternative omits references to the effective APR, as the Board would not require it to be disclosed on periodic statements.

C. *Calculation Methods*. The Board provides a variety of calculation methods depending on the types of charges assessed. § 226.14(d).

D. *List of Finance Charges Included in Calculation.* An issuer must include only the following finance charges for purposes of an effective APR calculation:

1. Charges attributable to a periodic rate used to calculate interest;

2. Charges that relate to a specific transaction;

3. Charges related to required credit insurance, debt cancellation, or debt suspension coverage;

4. Minimum charges imposed in limited circumstances; and

5. Charges based on the account balance, account activity or inactivity, or the amount of credit available. § 226.14(e)(1).

E. *Finance Charges Not Included in Calculation.* An issuer must not include the following finance charges for purposes of an effective APR calculation:

1. A charge related to opening the account; or

2. A charge related to continuing or renewing the account and imposed not more often than annually. § 226.14(e)(2).

XIV. § 226.16 Advertising.

A. *Trigger Terms*. Currently, for advertisements of open-end (not home-secured) plans, only positive terms trigger additional disclosure requirements. The Proposal would include terms stated negatively (*e.g.*, "no interest"). § 226.16(b)(1) and Comment 16(b)-1.

B. *Minimum Monthly Payments*.

1. If an advertisement for credit to finance the purchase of specific goods or services states a minimum monthly payment, the advertisement must also state the total of payments and the time period to repay the obligation, assuming that the consumer makes only the minimum payments.

2. The disclosures required must be equally prominent to the statement of the minimum monthly payment. § 226.16(b)(2).

C. *Introductory Rates*.

1. *Scope*. The introductory rate disclosure requirements apply to any written or electronic advertisement of an open-end (not home-secured) plan. § 226.16(e)(1).

2. *Use of "Introductory" or "Intro"*. If any APR that may be applied to the account is an introductory rate (*i.e.*, is less than the advertised APR that will be in effect at the end of the introductory period), the term "introductory" or "intro" must be in immediate proximity to each listing of the introductory rate. § 226.16(e)(2) and (3).

a. *"Immediate Proximity"*. The Board provides a safe harbor for issuers that place the word "introductory" or "intro" within the same phrase as each listing of the temporary APR. Comment 16(e)-2.

3. *Additional Disclosures*. If any APR that may be applied to the account is an introductory rate, the following must be stated in a clear and conspicuous manner in a prominent location closely proximate to the first listing of the introductory rate:

a. When the introductory rate will end; and

b. The APR that will apply at the end of the introductory period.

c. *"Prominent Location Closely Proximate"*. The Board provides a safe harbor for issuers that place the time period in which the introductory rate will end and the APR that will apply in the same paragraph as the first listing of the introductory rate. Comment 16(e)-3.

d. *"First Listing"*. The "first listing" is the most prominent listing of the introductory rate on the front of the "principal promotional document." If there is no reference to the temporary APR in the principal promotional document, the disclosures must appear in the first listing in each separate document in which the temporary APR does appear. Comment 16(e)-4.

4. *Envelope Excluded*. The requirement to state the end date for an introductory rate and the subsequent APR does not apply to an envelope or other enclosure in which an application or solicitation is mailed, or to a banner advertisement or pop-up advertisement linked to an application or solicitation provided electronically. § 226.16(e)(5).

D. *Fixed Rates*. An advertisement may not refer to an APR as "fixed" or use a similar term unless the advertisement also specifies a time period that the rate will be fixed and the rate will not increase during that period, or if no such time is provided, the rate will not increase while the plan is open. § 226.16(g).

XV. Miscellaneous.

A. *Open-End Plan*. The Board clarifies that, in general, a credit line is self-replenishing (and therefore eligible to be considered "open-end") if a consumer can obtain further advances or funds without being required to separately apply for those additional advances, and without undergoing a separate review by the creditor of that consumer's credit information, in order to obtain approval for each such additional advance. To perform a credit inquiry for each specific credit request would more closely resemble underwriting of closed-end credit. Comment 2(a)(20)-5.

"The Private Student Loan Transparency and Improvement Act"
June 8, 2007

The Dodd legislation extends new protections to all private student loans in order to improve transparency, prevent unfair and deceptive private lending practices and eliminate conflicts of interest.

Preventing Unfair and Deceptive Private Lending Practices and Eliminating Conflicts of Interest: The Dodd legislation draws from the New York State Code of Conduct and applies provisions of it to the private student loan market. The Dodd bill would:

- Prohibit lenders from engaging in revenue-sharing and loan co-branding arrangements that use the name or logo of an institution;
- Prohibit lenders from offering inducements, or any item of value, in exchange for preferential consideration of their private loan products or services;
- Prohibit lenders from using any data in their underwriting that may have disparate impact on the loan products, terms, or conditions available to student borrowers based on race, age, and other personal factors, or the institution they attend.

Improved Disclosures to Student Borrowers: Borrowers are best served when provided with accurate and timely disclosures about their private student loans. The Dodd legislation would:

- Require all private student loan solicitations to include a disclosure box that includes the loan's APR, other information regarding the terms and conditions of the loan, whether the rate is introductory or promotional, and if so, its duration;
- Require lenders to provide a clear and concise disclosure of the rate, terms and conditions of a private loan that has been approved for a student borrower *prior* to their signing the promissory note; and provides borrowers with a "cooling off" period;
- Requires lenders to provide prominent disclosure to applicants of their eligibility for lower-cost federal loans through the federal financial aid program and requires the borrower, and co-signor, to certify that they have received, and read, the disclosure;
- Apply Truth in Lending Act (TILA) provisions to *all* private student loans

Promoting Loan Transparency: The Dodd bill would authorize the Federal Reserve to implement rules requiring private lenders to collect and report data regarding their student loan applications, originations and denials, including the terms and conditions of the loans they make, aggregated by the race, gender, and age of the borrower as well as by type of institution. Similar requirements exist for mortgage lending activities under the Home Mortgage Disclosure Act (HMDA), which was enacted to curb discriminatory mortgage lending practices.

Making College More Affordable: The Dodd bill would authorize federal banking regulators to give financial institutions credit under the Community Reinvestment Act (CRA) for making "low-cost" private loans (i.e. loans with costs and fess similar to federally guaranteed loans) to low-income student borrowers.

SAMPLE LETTER

June 7, 2007

Charles Elliott (C.E.) Andrews
Chief Executive Officer
Sallie Mae Corporation
12061 Bluemont Way
Reston, VA 20190

Dear Mr. Andrews:

As you may know, the Office of the New York State Attorney General is currently conducting a nationwide investigation of the student loan industry. In addition, the United States Senate Committee on Banking, Housing, and Urban Affairs is presently conducting oversight of the private student loan market and the supervision of the private loan market by federal banking regulators. We are troubled by a number of industry practices which have already surfaced, ranging from conflicts of interest to kickback schemes to consumer frauds. We have now expanded our respective examinations to include criteria used by student loan providers to underwrite private education loans. We are coordinating our efforts to ensure an expeditious, comprehensive, and efficient resolution of our inquiries.

We have both learned from years of experience in the lending area that loan criteria can have powerful public policy and legal ramifications. Given our previously stated concerns, we believe that the criteria used for making private educational loans should be scrutinized as carefully and as extensively as the loan criteria used in the mortgage lending arena. Indeed, just yesterday in the Senate Banking Committee, one major private student lender testified that it uses data as part of its loan underwriting criteria that may disparately impact borrowers based upon their race.

To discharge our duties to investigate, remedy, and prevent injustice in this arena, we require your immediate cooperation in providing us with the requested information. Accordingly, please submit to both our respective offices documents that reflect your institution's recent and, if recently, modified private education loan underwriting criteria, including but not limited to whether your company considers the following factors: college, college location, graduation rate, historic default rate, race, gender, age, parental income, credit history, and any and all other factors used or considered in underwriting determinations. Please also provide the relative weights given to the various factors, any and all algorithms utilized, and all software used in underwriting student loan terms and eligibility. Please also submit all historical data regarding the rates, terms and conditions made for all student loans issued over the past five years as well as all loan applications and relevant data for all loans rejected over the past five years. In order to enhance our review of this loan data information, please provide this information in a searchable computer format. Please provide the underwriting criteria information no later than June 15, 2007, and the historical loan data no later that June 21, 2007.

Please coordinate the production of these documents with Benjamin Lawsky, Deputy Counselor and Special Assistant to Attorney General Cuomo, and Lynsey Graham, Senior Counsel, U.S. Senate Banking Committee Chairman Chris Dodd.

We look forward to your prompt response.

Sincerely,

Christopher J. Dodd
Chairman
Committee on Banking, Housing, and Urban Affairs
United States Senate

Andrew M. Cuomo
Attorney General of
the State of New York

AMENDED IN SENATE JUNE 13, 2007

AMENDED IN ASSEMBLY MAY 10, 2007

AMENDED IN ASSEMBLY MAY 2, 2007

CALIFORNIA LEGISLATURE—2007–08 REGULAR SESSION

ASSEMBLY BILL No. 1723

Introduced by Committee on Judiciary (Jones (Chair), Evans, Feuer, Krekorian, Laird, Levine, and Lieber)

March 6, 2007

An act to amend Sections 6091.2, 6211, 6212, and 6213 of the Business and Professions Code, relating to attorneys.

LEGISLATIVE COUNSEL'S DIGEST

AB 1723, as amended, Committee on Judiciary. Attorneys: IOLTA accounts.

Existing law, the State Bar Act, provides for the licensing and regulation of the practice of law by the State Bar of California. Existing law requires an attorney or law firm that receives or disburses trust funds to establish an interest bearing demand trust account and to deposit in the account all client deposits that are nominal in amount or are on deposit for a short period of time. Existing law requires the account to be established with a bank or other financial institution authorized by the Supreme Court, and requires the depository institution to meet certain requirements, including transmitting a remittance statement to the Supreme Court. Existing law requires that the earnings from these trust accounts be paid to the State Bar to be used for programs for free legal services for indigent persons.

This bill would instead require that the above funds be deposited in IOLTA accounts, and would require that the dividends earned on the

accounts be paid to the State Bar of California in the same manner as interest. The bill would require an IOLTA account to be established and maintained with an eligible institution, as defined, offering or making available an IOLTA account meeting specified requirements, including offering a rate of interest or dividends not less than that generally paid to nonattorney customers on similar accounts. The bill would authorize an eligible institution to charge only reasonable fees in accordance with customary practice, and would make any fees or service charges the sole responsibility of the lawyer or law firm maintaining the IOLTA account and payable only from the interest or dividends on the account, as specified. The bill would require an eligible institution's remittance statement to include the average balance for each account for each month. The bill would also make related changes.

Vote: majority. Appropriation: no. Fiscal committee: no. State-mandated local program: no.

The people of the State of California do enact as follows:

SECTION 1. Section 6091.2 of the Business and Professions Code is amended to read:

6091.2. As used in Section 6091.1:

(a) "Financial institution" means a bank, savings and loan, or other financial institution serving as a depository for attorney trust accounts under subdivision (a) or (b) of Section 6211.

(b) "Properly payable" means an instrument that, if presented in the normal course of business, is in a form requiring payment under the laws of this state.

(c) "Notice of dishonor" means the notice that a financial institution is required to give, under the laws of this state, upon presentation of an instrument that the institution dishonors.

SEC. 2. Section 6211 of the Business and Professions Code is amended to read:

6211. (a) An attorney or law ~~firm, which~~ *firm that*, in the course of the practice of law, receives or disburses trust funds~~,~~ shall establish and maintain an IOLTA account in which the attorney or law firm shall deposit or invest all client deposits or funds that are nominal in amount or are on deposit or invested for a short period of time. All such client funds may be deposited or invested in a single unsegregated account. The interest and

dividends earned on all those accounts shall be paid to the State Bar of California to be used for the purposes set forth in this article.

(b) Nothing in this article shall be construed to prohibit an attorney or law firm from establishing one or more interest bearing bank trust deposit accounts or dividend-paying trust investment accounts as may be permitted by the Supreme Court, with the interest or dividends earned on the accounts payable to clients for trust funds not deposited or invested in accordance with subdivision (a).

(c) With the approval of the Supreme Court, the State Bar may formulate and enforce rules of professional conduct pertaining to the use by attorneys or law firms of an IOLTA account for unsegregated client funds pursuant to this article.

(d) Nothing in this article shall be construed as affecting or impairing the disciplinary powers and authority of the Supreme Court or of the State Bar or as modifying the statutes and rules governing the conduct of members of the State Bar.

SEC. 3. Section 6212 of the Business and Professions Code is amended to read:

6212. An attorney who, or a law firm that, establishes an IOLTA account pursuant to subdivision (a) of Section 6211 shall comply with all of the following provisions:

(a) The IOLTA account shall be established and maintained with an eligible institution offering or making available an IOLTA account that meets the requirements of this article. The IOLTA account shall be established and maintained consistent with the attorney or law firm's duties of professional responsibility. An eligible financial institution shall have no responsibility for selecting the deposit or investment product chosen for the IOLTA account.

(b) Except as provided in subdivision (e), the rate of interest or dividends payable on any IOLTA account shall not be less than the interest rate or dividends generally paid by the eligible institution to nonattorney customers on accounts of the same type meeting the same minimum balance and other eligibility requirements as the IOLTA account. In determining the interest rate or dividend payable on any IOLTA account, an eligible institution may consider, in addition to the balance in the IOLTA account, risk or other factors customarily considered by the eligible institution when setting the interest rate or dividends for its

non-IOLTA accounts, provided that the factors do not discriminate between IOLTA customers and non-IOLTA customers and that these factors do not include the fact that the account is an IOLTA account. The eligible institution shall calculate interest and dividends in accordance with its standard practice for non-IOLTA customers. Nothing in this article shall preclude an eligible institution from paying a higher interest rate or dividend on an IOLTA account or from electing to waive any fees and service charges on an IOLTA account.

(c) Reasonable fees may be deducted from the interest or dividends remitted on an IOLTA account only at the rates and in accordance with the customary practices of the eligible institution for non-IOLTA customers. No other fees or service charges may be deducted from the interest or dividends earned on an IOLTA account. Unless and until the State Bar enacts regulations exempting from compliance with subdivision (a) of Section 6211 those accounts for which maintenance fees exceed the interest or dividends paid, an eligible institution may deduct the fees and service charges in excess of the interest or dividends paid on an IOLTA account from the aggregate interest and dividends remitted to the State Bar. Any fees and service charges other than reasonable fees shall be the sole responsibility of, and may only be charged to, the lawyer or law firm maintaining the IOLTA account. No fees or charges may be assessed against or deducted from the principal of any IOLTA account. It is the intent of the Legislature that the State Bar develop policies so that eligible institutions not incur uncompensated administrative costs in adapting their systems to comply with the provisions of Assembly Bill 1723 of the 2007–08 Regular Session or in making investment products available to IOLTA members.

(d) The eligible institution shall be directed to do all of the following:

(1) To remit interest or dividends on the IOLTA account, less reasonable fees, to the State Bar, at least quarterly.

(2) To transmit to the State Bar with each remittance a statement showing the name of the attorney or law firm for whom the remittance is sent, for each account the rate of interest applied or dividend paid, the amount and type of fees deducted, if any, and the average balance for each account for each month of the period for which the report is made.

(3) To transmit to the attorney or law firm customer at the same time a report showing the amount paid to the State Bar for that period, the rate of interest or dividend applied, the amount of fees and service charges deducted, if any, and the average daily account balance for each month of the period for which the report is made.

(e) An eligible institution has no affirmative duty to offer or make investment products available to IOLTA customers. However, if an eligible institution offers or makes investment products available to non-IOLTA customers, in order to remain an IOLTA eligible institution, it shall make those products available to IOLTA customers or pay an interest rate on the IOLTA deposit account that is comparable to the rate of return or the dividends generally paid on that investment product for similar customers meeting the same minimum balance and other requirements applicable to the investment product. If the eligible institution elects to pay that higher interest rate, the eligible institution may subject the IOLTA deposit account to equivalent fees and charges assessable against the investment product.

SEC. 4. Section 6213 of the Business and Professions Code is amended to read:

6213. As used in this article:

(a) "Qualified legal services project" means either of the following:

(1) A nonprofit project incorporated and operated exclusively in California which provides as its primary purpose and function legal services without charge to indigent persons and which has quality control procedures approved by the State Bar of California.

(2) A program operated exclusively in California by a nonprofit law school accredited by the State Bar of California which meets the requirements of subparagraphs (A) and (B).

(A) The program shall have operated for at least two years at a cost of at least twenty thousand dollars ($20,000) per year as an identifiable law school unit with a primary purpose and function of providing legal services without charge to indigent persons.

(B) The program shall have quality control procedures approved by the State Bar of California.

(b) "Qualified support center" means an incorporated nonprofit legal services center, which has as its primary purpose and function the provision of legal training, legal technical assistance, or advocacy support without charge and which actually provides

through an office in California a significant level of legal training, legal technical assistance, or advocacy support without charge to qualified legal services projects on a statewide basis in California.

(c) "Recipient" means a qualified legal services project or support center receiving financial assistance under this article.

(d) "Indigent person" means a person whose income is (1) 125 percent or less of the current poverty threshold established by the United States Office of Management and Budget, or (2) who is eligible for Supplemental Security Income or free services under the Older Americans Act or Developmentally Disabled Assistance Act. With regard to a project which provides free services of attorneys in private practice without compensation, "indigent person" also means a person whose income is 75 percent or less of the maximum levels of income for lower income households as defined in Section 50079.5 of the Health and Safety Code. For the purpose of this subdivision, the income of a person who is disabled shall be determined after deducting the costs of medical and other disability-related special expenses.

(e) "Fee generating case" means any case or matter that, if undertaken on behalf of an indigent person by an attorney in private practice, reasonably may be expected to result in payment of a fee for legal services from an award to a client, from public funds, or from the opposing party. A case shall not be considered fee generating if adequate representation is unavailable and any of the following circumstances exist:

(1) The recipient has determined that free referral is not possible because of any of the following reasons:

(A) The case has been rejected by the local lawyer referral service, or if there is no such service, by two attorneys in private practice who have experience in the subject matter of the case.

(B) Neither the referral service nor any attorney will consider the case without payment of a consultation fee.

(C) The case is of the type that attorneys in private practice in the area ordinarily do not accept, or do not accept without prepayment of a fee.

(D) Emergency circumstances compel immediate action before referral can be made, but the client is advised that, if appropriate and consistent with professional responsibility, referral will be attempted at a later time.

(2) Recovery of damages is not the principal object of the case and a request for damages is merely ancillary to an action for equitable or other nonpecuniary relief, or inclusion of a counterclaim requesting damages is necessary for effective defense or because of applicable rules governing joinder of counterclaims.

(3) A court has appointed a recipient or an employee of a recipient pursuant to a statute or a court rule or practice of equal applicability to all attorneys in the jurisdiction.

(4) The case involves the rights of a claimant under a publicly supported benefit program for which entitlement to benefit is based on need.

(f) "Legal Services Corporation" means the Legal Services Corporation established under the Legal Services Corporation Act of 1974 (Public Law 93-355; 42 U.S.C. Sec. 2996 et seq.).

(g) "Older Americans Act" means the Older Americans Act of 1965, as amended (Public Law 89-73; 42 U.S.C. Sec. 3001 et seq.).

(h) "Developmentally Disabled Assistance Act" means the Developmentally Disabled Assistance and Bill of Rights Act of 1975, as amended (Public Law 94-103; 42 U.S.C. Sec. 6001 et seq.).

(i) "Supplemental security income recipient" means an individual receiving or eligible to receive payments under Title XVI of the federal Social Security Act, or payments under Chapter 3 (commencing with Section 12000) of Part 3 of Division 9 of the Welfare and Institutions Code.

(j) "IOLTA account" means *an account or investment product established and maintained pursuant to subdivision (a) of Section 6211 that is* any of the following:

(1) An interest-bearing checking account.

(2) An investment sweep product that is a daily (overnight) financial institution repurchase agreement or an open-end money-market fund.

(3) Any other investment product authorized by California ~~Supreme Court rule or order and established and maintained pursuant to subdivision (a) of Section 6211.~~ *Supreme Court rule or order.*

A daily financial institution repurchase agreement shall be fully collateralized by United States Government Securities or other comparably conservative debt securities, and may be established only with any eligible institution that is "well-capitalized" or

"adequately capitalized" as those terms are defined by applicable federal statutes and regulations. An open-end money-market fund shall be invested solely in United States Government Securities or repurchase agreements fully collateralized by United States Government Securities *or other comparably conservative debt securities*, shall hold itself out as a "money-market fund" as that term is defined by federal statutes and regulations under the Investment Company Act of 1940 (15 U.S.C. Sec. 80a-1 et seq.), and, at that time of the investment, shall have total assets of at least two hundred fifty million dollars ($250,000,000).

(k) "Eligible institution" means a bank or any other type of financial institution authorized by the Supreme Court.

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Filed 6/4/07

IN THE SUPREME COURT OF CALIFORNIA

ZENGEN, INC.,	
Plaintiff and Appellant,	
v.	S142947
COMERICA BANK,	Ct.App. 2/5 B179022
Defendant and Respondent.	Los Angeles County Super. Ct. No. BC290637

It appears the chief financial officer of a company embezzled $4.6 million by directing four fraudulent funds transfers from the company's account to an account he controlled. He has disappeared with the money. The ultimate question in this litigation is who must bear the loss: the bank that honored the fraudulent payment orders or the company that employed the embezzler. We granted review to decide two questions arising under California's Uniform Commercial Code (hereafter, sometimes, California Code).[1]

First, we must decide whether a cause of action under the California Uniform Commercial Code displaces other common law causes of action such that the company must recover from the bank under the California Code or not at all. Because the California Code provides detailed rules and procedures concerning

[1] All statutory citations are to the California Uniform Commercial Code unless otherwise indicated. Division 11 of that code (division 11), the part relevant to this case, is identical to article 4A of the Uniform Commercial Code (article 4A). (See pt. II, *post*.)

funds transfers that squarely cover the transactions at issue, we conclude that the California Code does displace common law causes of action.

Second, as a prerequisite to recovering from the bank, the customer must "notif[y] the bank of the customer's objection to the payment within one year after" the customer received payment notification. (§ 11505.) We must decide exactly what objection the customer must convey to the bank. Reading the statute in context, we conclude that the customer must not merely inform the bank that the payment orders were unauthorized or fraudulent; it must inform the bank in some way that the customer objected to what the bank had done in accepting the payment orders. But the statute does not require any particular formulaic words. Rather, it is sufficient if, based on all of the circumstances, a reasonable bank would understand that the customer was objecting to what the bank had done in accepting the payment orders or otherwise considered the bank liable for the loss. We will remand the matter to the Court of Appeal to apply this test to the facts of the case.

I. FACTS AND PROCEDURAL HISTORY

Plaintiff Zengen, Inc. (Zengen) is a biopharmaceutical company formed in May 1999 with Johnson Liu as its chief executive officer and Fung Yen as its chief financial officer. Shortly after incorporating, it opened several bank accounts, including money market account No. 88-012-298 (the 298 Account), at Imperial Bank, which defendant Comerica Bank has since acquired.[2] In connection with the opening of these accounts, Liu and Yen executed a business signature card and a funds transfer authorization agreement. The authorization agreement did not specifically list the 298 Account by number, but Liu has

[2] We will refer to Imperial Bank and Comerica Bank collectively as the Bank.

acknowledged that the authorization applies to it. Liu and Yen were the company's authorized signatories.

While Liu had unlimited check signing authority, Yen's authority was limited to checks not exceeding $10,000. The funds transfer authorization agreement stated that "any transfer over $50,000, requires both CEO & CFO authorization." (Original underlining.) It listed Liu as Zengen's "CEO" and Yen as its "CFO." Next to the listings of both Liu and Yen as authorized persons was the annotation, "V & F." The agreement stated that "F = FAX" and "V = VERBAL."[3]

It appears that from mid-2000 to early 2001, Yen embezzled $4.6 million from Zengen by directing four funds transfers from the 298 Account to an account he controlled. To do so, he formed a British Virgin Islands corporation, which he named Zengen, Inc. He then opened an account at Chinatrust Bank in the name of this new corporation with an initial deposit of $1,000, with himself as the sole authorized signatory. Between July 11, 2000, and February 5, 2001, the Bank processed four payment orders, which are the subject matter of this lawsuit. It appeared on their face that Liu had signed and authorized the payment orders. As was customary, they were faxed to the Bank for processing and payment. The orders requested the Bank to draw funds out of the 298 Account and to wire them to Zengen, Inc.'s account at Chinatrust Bank in the amounts and on the dates as follows: $185,000 on July 11, 2000; $550,000 on September 11, 2000; $1,500,000 on November 22, 2000; and $1,700,000 on February 5, 2001. The

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[3] In its brief in this court, Zengen stated that this agreement meant that "[b]oth Liu and Yen had to sign and verbally confirm any request for wire transfers over $50,000.00." The Bank did not dispute this interpretation of the funds transfer authorization agreement in its brief, but at oral argument it stated it had a different interpretation. If they think it appropriate, the parties may pursue this point on remand.

Bank processed the payment orders and debited the 298 Account for these transactions. The transactions appeared on Zengen's monthly bank statements, which Zengen acknowledges it received.

Zengen's account statements and transaction notices were addressed to Yen as the company's chief financial officer. Probably for this reason, the company did not immediately discover Yen's actions. Zengen first learned that something was wrong on June 13, 2001. After that date, Zengen's office manager, Regina Samuel-Ramcharitar, worked with Tony Galvez of the Bank to uncover the unauthorized activity concerning the 298 Account.

Samuel-Ramcharitar's declaration states the following. Sometime before June 27, 2001, she told Galvez that "Zengen had not been aware of the transfer of the funds, that Mr. Liu had not signed the wire transfer request, that Mr. Yen himself had no authority to transfer the funds, that the wire transfer request was fraudulent and had not been authorized by Zengen, and that Zengen believed that Mr. Yen had stolen the money." On July 10 or 11, after further investigation, she additionally told Galvez that Zengen "had received microfilm documents from Chinatrust Bank showing additional wire transfers from Imperial Bank to Chinatrust Bank, gave him the dates and amounts set forth above, and told him that these transfers, like the transfer of the $1,700,000.00 on February 5, 2001, were fraudulent and unauthorized, that it appeared that Mr. Yen had stolen this money as well, and asked him to obtain for us the bank's documentation on those transfers. In this and in all my conversations with Mr. Galvez, I continued to keep Mr. Galvez apprised of the facts as we learned them concerning Mr. Yen's fraudulent transfers of funds from the Zengen account at Imperial Bank to the supposed Zengen account at Chinatrust Bank. By July 12, 2001, I had specifically told Mr. Galvez that Zengen did not authorize the four wire transfers [at issue] and that it appeared that Yen had fraudulently transferred the money."

Liu testified in a deposition that sometime in June, 2001, he told Julie Yen,[4] a Bank official, "I didn't authorize any of those transactions. I suspect that he [Yen] must have cut and paste[d] my signature if you saw both signatures in there." He also testified that he also spoke with Julie Yen at a restaurant in Monterey Park. He could not remember when this conversation occurred. When he was asked at the deposition, "Do you recall what, if anything, Ms. Yen said to you?" Liu responded, "No. It's just very general discussion, you know, about bank being sued. And she was just trying to find out—I think she was just trying to find out what has been going on."

By August 2001, when Zengen filed a report with the Los Angeles District Attorney's office which included details of the four unauthorized payment orders, Zengen had concluded that Yen had stolen money from the company by ordering the wire transfers from the 298 Account to the Chinatrust Bank. By that time Yen had disappeared with the company's financial records and could not be located.

On February 20, 2003, Zengen filed the instant lawsuit against the Bank and other parties. It claims the Bank is liable for the $4.6 million loss because it should not have accepted the four unauthorized payment orders. The complaint alleged causes of action against the Bank for breach of contract, negligence, a refund of payment under section 11204, return of deposit, and money had and received. The Bank demurred. The trial court sustained the demurrer without leave to amend to the negligence cause of action on the ground that the California Uniform Commercial Code had displaced a negligence claim. Ultimately, after the complaint was amended, the trial court denied the demurrer to the other causes of action. However, the court later granted summary judgment in the Bank's favor on all of the remaining causes of action. It made two critical rulings: (1) The

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[4] Fung Yen and Julie Yen are no relation. To avoid confusion, we will refer to Julie Yen by both her first and last names.

California Code had displaced the non California Uniform Commercial Code causes of action; and (2) Zengen could not prevail on its California Code claim because it failed to notify the Bank of its objection to the payments within the time that section 11505 prescribes.

Zengen appealed. The Court of Appeal affirmed. The majority, in an opinion authored by Acting Presiding Justice Armstrong, agreed with both of the trial court's rulings. Justice Mosk dissented. He agreed that the California Code displaced Zengen's common law causes of action. However, he believed that Zengen adequately notified the Bank of its objection within the meaning of section 11505, and, therefore, the trial court should not have granted summary judgment on the California Code cause of action.

We granted Zengen's petition for review.

II. DISCUSSION

"The 1990 Legislature enacted Article 4A of the Uniform Commercial Code as Division 11 of the California Uniform Commercial Code (U.C.C. 11101 et seq.), entitled 'Funds Transfers.' " (4 Witkin, Summary of Cal. Law (10th ed. 2005) Negotiable Instruments, § 132, p. 505.) In one of its causes of action, Zengen seeks from the Bank a refund of the fraudulently transferred funds under these provisions. Zengen also seeks recovery from the bank under various other causes of action. The issues before us on review are whether (1) the California Uniform Commercial Code displaces the remaining causes of action, and (2) Zengen is precluded from recovering under the California Uniform Commercial Code because it failed to notify the Bank in time of its objection to the payments.[5]

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[5] The parties sometimes use the word "preempt" rather than "displace" in discussing what effect the California Code has on the other causes of action. Technically, the doctrine of preemption concerns whether a federal law has superseded a state law or a state law has superseded a local law, not whether one provision of state law has displaced other provisions of state law. (See *Stop Youth*

To place these issues into context, we will first review the relevant portions of division 11 of the California Uniform Commercial Code and their general application to this case. Then we will discuss the two issues in order.

A. Division 11 of the California Uniform Commercial Code

With one exception not relevant here, division 11 of the California Code applies to "funds transfers defined in Section 11104." (§ 11102.)[6] As relevant here, section 11104, subdivision (a), defines a "funds transfer" as "the series of transactions, beginning with the originator's payment order, made for the purpose of making payment to the beneficiary of the order."[7]

Section 11103 defines other terms important to understanding these issues:

"(a) In this division:

"(1) 'Payment order' means an instruction of a sender to a receiving bank, transmitted orally, electronically, or in writing, to pay, or to cause another bank to pay, a fixed or determinable amount of money to a beneficiary if all of the following apply:

"(i) The instruction does not state a condition to payment to the beneficiary other than time of payment.

Addiction, Inc. v. Lucky Stores, Inc. (1998) 17 Cal.4th 553, 568; see also § 1103 [using the word "displaced"].) Here, the California Code and other causes of action are all matters of state law. Accordingly, we will use the word "displace" in discussing this issue.

[6] Division 11 does not apply to funds transfers governed by the Electronic Fund Transfer Act of 1978, title 15 United States Code section 1693, et seq., which concerns consumer accounts. (§§ 11102, 11108.)

[7] In its entirety, section 11104, subdivision (a), provides: " 'Funds transfer' means the series of transactions, beginning with the originator's payment order, made for the purpose of making payment to the beneficiary of the order. The term includes any payment order issued by the originator's bank or an intermediary bank intended to carry out the originator's payment order. A funds transfer is completed by acceptance by the beneficiary's bank of a payment order for the benefit of the beneficiary of the originator's payment order."

"(ii) The receiving bank is to be reimbursed by debiting an account of, or otherwise receiving payment from, the sender.

"(iii) The instruction is transmitted by the sender directly to the receiving bank or to an agent, funds-transfer system, or communication system for transmittal to the receiving bank.

"(2) 'Beneficiary' means the person to be paid by the beneficiary's bank.

"(3) 'Beneficiary's bank' means the bank identified in a payment order in which an account of the beneficiary is to be credited pursuant to the order or which otherwise is to make payment to the beneficiary if the order does not provide for payment to an account.

"(4) 'Receiving bank' means the bank to which the sender's instruction is addressed.

"(5) 'Sender' means the person giving the instruction to the receiving bank.

"(b) If an instruction complying with paragraph (1) of subdivision (a) is to make more than one payment to a beneficiary, the instruction is a separate payment order with respect to each payment.

"(c) A payment order is issued when it is sent to the receiving bank."

Under these definitions, it seems clear, and the parties do not dispute, that the four transactions involved in this case were funds transfers and, accordingly, division 11 of the California Uniform Commercial Code applies to them. (§ 11102.) The four orders requesting the Bank to draw funds out of the 298 Account and to wire them to the account at Chinatrust Bank were payment orders. Plaintiff Zengen was the sender. Defendant Bank was the receiving bank. The account that Yen opened at Chinatrust Bank under the name "Zengen, Inc.," was the beneficiary. The Bank was reimbursed for crediting the beneficiary account by debiting Zengen's account. Chinatrust Bank was the beneficiary's bank.

Section 11202, subdivision (a), provides: "A payment order received by the receiving bank is the authorized order of the person identified as sender if that person authorized the order or is otherwise bound by it under the law of agency." Zengen alleges and, on review of summary judgment, we must accept as true, that the payment orders at issue were not authorized under this subdivision.

However, section 11202, subdivision (b), provides: "If a bank and its customer have agreed that the authenticity of payment orders issued to the bank in the name of the customer as sender will be verified pursuant to a security procedure[8], a payment order received by the receiving bank is effective as the order of the customer, whether or not authorized, if (i) the security procedure is a commercially reasonable method of providing security against unauthorized payment orders, and (ii) the bank proves that it accepted the payment order in good faith and in compliance with the security procedure and any written agreement or instruction of the customer restricting acceptance of payment orders issued in the name of the customer. The bank is not required to follow an instruction that violates a written agreement with the customer or notice of which is not received at a time and in a manner affording the bank a reasonable opportunity to act on it before the payment order is accepted."

Under section 11202, subdivision (b), if a bank accepts an unauthorized payment order in good faith, it is not liable if a commercially reasonable security

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8 Section 11201 defines a "security procedure" as "a procedure established by agreement of a customer and a receiving bank for the purpose of (i) verifying that a payment order or communication amending or canceling a payment order is that of the customer, or (ii) detecting error in the transmission or the content of the payment order or communication. A security procedure may require the use of algorithms or other codes, identifying words or numbers, encryption, callback procedures, or similar security devices. Comparison of a signature on a payment order or communication with an authorized specimen signature of the customer is not by itself a security procedure."

procedure was in place, and the bank followed it and any other applicable written agreement or instruction of the customer. (See 3 White & Summers, Uniform Commercial Code (4th ed. 1995) § 24-5, p. 79.) Zengen alleges that the Bank did not follow the security procedure that was in place because it did not obtain verbal authorization from Liu, as the funds transfer authorization agreement required. Because the trial court granted summary judgment for the Bank on other grounds, this question has not been litigated in this case.

Section 11204, subdivision (a), provides: "If a receiving bank accepts a payment order issued in the name of its customer as sender which is (i) not authorized and not effective as the order of the customer under Section 11202, or (ii) not enforceable, in whole or in part, against the customer under Section 11203[9], the bank shall refund any payment of the payment order received from the customer to the extent the bank is not entitled to enforce payment and shall pay

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9 Section 11203 provides: "(a) If an accepted payment order is not, under subdivision (a) of Section 11202, an authorized order of a customer identified as sender, but is effective as an order of the customer pursuant to subdivision (b) of Section 11202, the following rules apply:

"(1) By express written agreement, the receiving bank may limit the extent to which it is entitled to enforce or retain payment of the payment order.

"(2) The receiving bank is not entitled to enforce or retain payment of the payment order if the customer proves that the order was not caused, directly or indirectly, by a person (i) entrusted at any time with duties to act for the customer with respect to payment orders or the security procedure, or (ii) who obtained access to transmitting facilities of the customer or who obtained, from a source controlled by the customer and without authority of the receiving bank, information facilitating breach of the security procedure, regardless of how the information was obtained or whether the customer was at fault. Information includes any access device, computer software, or the like.

"(b) This section applies to amendments of payment orders to the same extent it applies to payment orders."

It is not clear that this section is relevant to this case although, as noted, the trial court granted summary judgment on other grounds so questions such as this have not been litigated.

interest on the refundable amount calculated from the date the bank received payment to the date of the refund. However, the customer is not entitled to interest from the bank on the amount to be refunded if the customer fails to exercise ordinary care to determine that the order was not authorized by the customer and to notify the bank of the relevant facts within a reasonable time not exceeding 90 days after the date the customer received notification from the bank that the order was accepted or that the customer's account was debited with respect to the order. The bank is not entitled to any recovery from the customer on account of a failure by the customer to give notification as stated in this section." Zengen is seeking a refund from the Bank under this provision.

Section 11505 provides that the customer must notify the bank within one year after receiving notice of a payment order of its objection to the payment in order to obtain a refund. This provision is at the heart of the second issue before us on review.

B. Whether the California Uniform Commercial Code Displaces Zengen's non California Uniform Commercial Code Causes of Action

Zengen filed this lawsuit seeking reimbursement from the Bank for the $4.6 million that Yen caused the Bank to transfer to his account at Chinatrust Bank. One of its causes of action is for a refund under the California Uniform Commercial Code. It has also alleged common law causes of action for breach of contract, negligence, return of deposit, and money had and received. Zengen bases each cause of action on its claim that the Bank should not have accepted the fraudulent payment orders. We must decide whether the California Code has fully occupied the field of this litigation and displaced the non California Code causes of action.

The California Uniform Commercial Code does not automatically displace all other legal principles. Section 1103, which applies to the entire California Code, provides: "*Unless displaced by the particular provisions of this code*, the principles of law and equity, including the law merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplement its provisions." (Italics added.)

Thus, other principles of law will apply here unless some particular provisions of the California Uniform Commercial Code have displaced them. The Bank contends that division 11 has displaced the other causes of action. Section 11102 provides that division 11 "applies to funds transfers defined in Section 11104." The parties do not dispute that the funds transfers at issue here are funds transfers to which division 11 applies. The question before us, however, is not whether division 11 applies, but whether it applies *to the exclusion* of other legal principles giving rise to other causes of action.

As the Court of Appeal noted, "sections 11201 through 11204 provide a detailed scheme for analyzing the rights, duties and liabilities of banks and their customers in connection with the authorization and verification of payment orders. Analysis of a funds transfer under these sections results in a determination of whether or not the funds transfer was 'authorized,' and provides a very specific scheme for allocation of loss." The Uniform Commercial Code Comment (hereafter, sometimes, Code Comment) explains why this is so.

The Code Comment to section 4A-102, adopted in California as 11102, states: "In the drafting of Article 4A [i.e., division 11], a deliberate decision was made to write on a clean slate and to treat a funds transfer as a unique method of payment to be governed by unique rules that address the particular issues raised by this method of payment. A deliberate decision was also made to use precise and

detailed rules to assign responsibility, define behavioral norms, allocate risks and establish limits on liability, rather than to rely on broadly stated, flexible principles. In the drafting of these rules, a critical consideration was that the various parties to funds transfers need to be able to predict risk with certainty, to insure against risk, to adjust operational and security procedures, and to price funds transfer services appropriately. This consideration is particularly important given the very large amounts of money that are involved in funds transfers.

"Funds transfers involve competing interests—those of the banks that provide funds transfer services and the commercial and financial organizations that use the services, as well as the public interest. These competing interests were represented in the drafting process and they were thoroughly considered. *The rules* that emerged represent a careful and delicate balancing of those interests and *are intended to be the exclusive means* of determining the rights, duties and liabilities of the affected parties *in any situation covered by particular provisions* of the Article. *Consequently, resort to principles of law or equity outside of Article 4A is not appropriate to create rights, duties and liabilities inconsistent with those stated in this Article*." (Code Com., reprinted at 23D West's Ann. Cal. U. Com. Code (2002) foll. § 11102, pp. 27-28, italics added.)

Because, in enacting division 11, the Legislature adopted article 4A of the Uniform Commercial Code exactly as written, this Code Comment is persuasive in interpreting the statute. (See *People v. Martinez* (2000) 22 Cal.4th 106, 129 [comments of the Law Revision Commission are persuasive of Legislative intent when the Legislature adopts a law exactly as the commission proposed].)

Witkin explains the need that existed for a comprehensive statute: "The focus of [article 4A] is a type of payment, commonly referred to as a 'wholesale wire transfer,' which is used almost exclusively between business or financial institutions. Payments made by wire transfer, as distinguished from payments

made by checks or credit cards, or from electronically based consumer payments, require a separate body of law that addresses the unique operational and policy issues presented by the method. *It was therefore the intent of the drafters of Article 4A to provide a comprehensive body of law to govern the rights and obligations resulting from wire transfers.* [Citations.]

"A typical funds transfer involves a large amount of money, multimillion-dollar transactions being common. Most transactions are completed in a single day; thus, funds transfers are efficient substitutes for payments made by delivery of paper instruments. An additional feature is low cost, in that transfers involving millions of dollars can be made for a few dollars. However, in the event a problem arises, risk of loss to banks may be high. Thus, '*a major policy issue in the drafting of Article 4A is that of determining how risk of loss is to be allocated given the price structure in the industry.*' [Citation.]" (4 Witkin, Summary of Cal. Law, *supra*, § 132, p. 505, italics added.)

In light of these authorities, we agree with the Court of Appeal that "division 11 provides that common law causes of action based on allegedly unauthorized funds transfers are preempted in two specific areas: (1) where the common law claims would create rights, duties, or liabilities inconsistent with division 11; and (2) where the circumstances giving rise to the common law claims are specifically covered by the provisions of division 11."

Courts from other jurisdictions have reached similar conclusions in considering the provisions of article 4A. (*Grain Traders, Inc. v. Citibank, N.A.* (2d Cir. 1998) 160 F.3d 97, 103; *Community Bank, FSB v. Stevens Financial Corp.* (N.D.Ind. 1997) 966 F.Supp. 775, 788; *Impulse Trading v. Norwest Bank Minn., N.A.* (D.Minn. 1995) 907 F.Supp. 1284, 1287-1288; *Fitts v. Amsouth Bank* (Ala. 2005) 917 So.2d 818, 824 ["if the situation made the basis of a dispute is addressed in Article 4A, then the provisions of Article 4A provide the exclusive

rights and remedies of the parties involved"]; *Corfan Banco v. Ocean Bank* (Fla.Dist.Ct.App. 1998) 715 So.2d 967, 971; *Aleo Intern., LTD. v. Citibank, N.A.* (N.Y.Sup.Ct. 1994) 612 N.Y.S.2d 540; *Moody Nat. Bank v. Texas City Development* (Tex.Ct.App. 2001) 46 S.W.3d 373, 377-379.) As one court observed, "The uniformity and certainty sought by the statute for these transactions could not possibly exist if parties could opt to sue by way of [pre-Uniform Commercial Code] remedies where the statute has specifically defined the duties, rights and liabilities of the parties." (*Corfan Banco v. Ocean Bank*, *supra*, at p. 971, fn. 5.)

This is not to say that the Uniform Commercial Code necessarily displaces all common law actions based on all activities surrounding funds transfers. One court has explained that "[t]he exclusivity of Article 4-A is deliberately restricted to 'any situation covered by particular provisions of the Article.' Conversely, situations not covered are not the exclusive province of the Article." (*Sheerbonnet, Ltd. v. American Exp. Bank, Ltd.* (S.D.N.Y. 1995) 951 F.Supp. 403, 407-408.) The *Sheerbonnet* court held that the Uniform Commercial Code did not displace causes of action based on a bank's crediting funds from a payment order to the account of an insolvent company even though the bank knew the account had been frozen, and then asserting its own rights to the funds as an off-set against debts owed to it by the insolvent account holder. (*Id*. at pp. 405.) It concluded that no portion of the Uniform Commercial Code "directly addresses the allegations" of the case. (*Id*. at p. 412.) (See also *Centre-Point Merchant Bank v. American Express* (S.D.N.Y. 1996) 913 F.Supp. 202, 205-208 [Uniform Commercial Code displaces common law cause of action based on acceptance of fraudulent payment orders but not one based on failure to follow certain "rollover instructions" that were neither a "payment order" nor a "funds transfer"]; *Schlegel v. Bank of America, N.A.* (Va. 2006) 628 S.E.2d 362, 368 [Uniform Commercial

Code displaces "common law claims as they relate to the alleged unauthorized payment orders" but not common law claims arising from the freezing of funds without refunding them to a certain bank account].)

Here, the gravamen of each of Zengen's causes of action against the Bank, including the one based on the California Uniform Commercial Code, is the same: The bank should not have accepted and executed the fraudulent payment orders. Primarily, it alleges the Bank violated the funds transfer authorization agreement by not obtaining verbal authorization from Liu. The California Code squarely covers the question who should bear the loss when a bank executes an unauthorized payment order. Zengen argues that the California Code does not cover its negligence cause of action because it alleges a number of circumstances that should have caused the Bank to become suspicious and discover the fraud, including the fact that the funds authorization agreement did not specifically list the 298 Account by number. It asserts that these facts "have nothing to do with the *transactional* aspects of funds transfers." We disagree. As the Court of Appeal explained, "Although the California Uniform Commercial Code does not catalog all the ways in which a bank may execute an unauthorized wire transfer, it certainly specifies the consequences for doing so. Section 11201 et seq. sets forth the respective rights, duties and liabilities of the parties upon the issuance and acceptance of a payment order under division 11." To adapt the conclusion of one court to this case, "[b]ecause the situation made the basis of the [plaintiff's] common-law claims—that [the Bank] made an improper funds transfer—is unequivocally addressed in the particular provisions of Article 4A, we conclude that those common-law claims are displaced by Article 4A and that the [plaintiff's] exclusive remedy for that claim must be found in Article 4A." (*Fitts v. Amsouth Bank*, *supra*, 917 So.2d at p. 824.)

Regarding its breach of contract cause of action, Zengen argues that the Bank contractually agreed to execute a payment order "only in strict accordance with Zengen's instructions," and that it breached this agreement. Again, the California Uniform Commercial Code covers this subject matter and this transaction; it provides specific rules and remedies for the failure to follow a security procedure. Zengen also notes that the California Code expressly states that "[e]xcept as otherwise provided in this division, the rights and obligations of a party to a funds transfer may be varied by agreement of the affected party." (§ 11501, subd. (a); see *Hedged Inv. Partners v. Norwest Bank Mn.* (Minn.Ct.App. 1998) 578 N.W.2d 765, 771 [Uniform Commercial Code does not displace contractual cause of action based on an agreement that "covers specific fiduciary responsibilities that go well beyond the scope of wire transfer services"].) We need not explore whether and how this provision might apply to the rights and obligations involved here. (See, e.g., *Regatos v. North Fork Bank* (N.Y.App.Div. 2005) 804 N.Y.S.2d 713 [one-year notification time period may not be modified by contract].) In this case, Zengen does not allege any contractual agreement to change the parties' rights and obligations to a funds transfer. It relies solely on the business signature card and funds transfer authorization agreement, neither of which contains any agreement to modify the California Code's provisions.[10]

"In sum," as the Court of Appeal concluded, "the facts of this case fall squarely within the provisions of division 11 of the California Uniform Commercial Code. This case is about unauthorized wire funds transfers. Zengen's non-California Uniform Commercial Code causes of action are based solely on the

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10 In support of its argument that division 11 does not displace its common law causes of action, Zengen also relies on *Sun'n Sand, Inc. v. United California Bank* (1978) 21 Cal.3d 671. That case involved different sections of the California Uniform Commercial Code and was decided over a decade before the Legislature enacted division 11. It is irrelevant to the proper interpretation of division 11.

analysis prescribed by division 11—that the Bank processed unauthorized payment orders. Because the California Uniform Commercial Code provides a remedy to Zengen under these circumstances, it preempts the common law causes of action alleged in the Zengen's complaint."

C. Whether Zengen Is Precluded from Recovering under the California Uniform Commercial Code Because It Failed to Notify the Bank in Time of its Objection

Section 11505 provides: "If a receiving bank has received payment from its customer with respect to a payment order issued in the name of the customer as sender and accepted by the bank, and the customer received notification reasonably identifying the order, the customer is precluded from asserting that the bank is not entitled to retain the payment unless the customer notifies the bank of *the customer's objection to the payment* within one year after the notification was received by the customer." (Italics added.) We must decide exactly what the italicized words mean. Specifically, we must decide whether (1) it suffices for the customer to notify the bank that the payment orders were unauthorized or fraudulent (Zengen's position), or (2) the customer must object to the bank's action in debiting the customer's account or otherwise receiving payment from the customer (the Bank's position).

We conclude that, properly understood, the Bank's legal position is correct. The customer need not precisely state in so many words that it objects to the debiting of its account, but it must inform the bank in some fashion it believes the bank should not have accepted the payment order or otherwise is liable for the loss. Under the California Uniform Commercial Code, a bank is not necessarily liable for accepting an unauthorized, or even fraudulent, payment order. Accordingly, merely informing the bank the payment order was fraudulent does not inform it that the customer considers it liable for the loss.

We begin our analysis with the Uniform Commercial Code Comment to section 4A-505, adopted in California as section 11505, which, as noted above, is highly persuasive in interpreting the statute. That Code Comment notes that section 11505 "is in the nature of a statute of repose for objecting to debits made to the customer's account." It explains that in some circumstances, the receiving bank may be obliged to refund a payment made pursuant to a customer's payment order. It concludes by stating, "Under 4A-505 [i.e., section 11505], however, the obligation to refund may not be asserted by the customer if the customer has not objected *to the debiting of the account* within one year after the customer received notification of the debit." (Code Com., reprinted at 23D West's Ann. Cal. U. Com. Code, *supra*, foll. § 11505, p. 110, italics added.) The italicized language indicates the customer must object to *what the bank did*, not merely inform the bank the payment order was unauthorized.

Moreover, as the Bank notes, section 11505 requires an objection to the "payment" not the "payment order." That section contains only one sentence. The sentence begins with the words, "If a receiving bank has received *payment* from its customer . . . ." (Italics added.) The portion at issue here requires the customer to notify the bank of its "objection to the *payment* . . . ." (Italics added.) In context, it is clear that both italicized words, "payment," refer to the same thing—the payment the bank received from its customer. Throughout this statutory scheme, the California Uniform Commercial Code distinguishes between the payment and the payment order. (See, e.g. § 11204 [referring to a refund of "any payment of the payment order"].) The Bank received this payment when it debited Zengen's 298 Account. (See § 11103, subd. (a)(1)(ii).) As indicated in the Code Comment to section 11505, it is this payment, that is, this debiting, to which the customer must object within one year of receiving notice of the payment order. Given the care with which the Uniform Commercial Code was drafted, and

the goal stated in the Code Comment to section 11102 to use throughout division 11 "precise and detailed rules," we must interpret section 11505 to mean what it says. Merely stating that the payment order was unauthorized is not enough.

This conclusion is bolstered by the fact that the California Uniform Commercial Code sometimes requires the customer to notify the bank "of the relevant facts" within a shorter period than one year or face certain consequences. The section that Zengen relies on in seeking a refund provides an example. Section 11204 generally requires a bank that is required to refund a payment also to pay interest on the payment from the date the bank received it to the date of the refund. However, in order to be entitled to this interest, the customer must exercise ordinary care and "notify the bank of the relevant facts within a reasonable time not exceeding 90 days" after the customer received notification of the payment. (See also § 11304 [another example of a "relevant facts" notification requirement].) Notifying the bank that the payment orders were fraudulent might be notifying it of the relevant facts, but section 11505's one-year notification requirement must mean something different than merely notifying the bank of the relevant facts. In context, the difference is that section 11505 requires notification that the bank may be liable for the loss.

Good reason exists for the California Uniform Commercial Code to require only that the customer inform the bank promptly—within 90 days at most—of the relevant facts in order to receive interest on the refund, but to require it to notify the bank of its objection to the bank's action within one year. Prompt notification of the relevant facts can ensure that the bank does not accept any additional unauthorized payment orders. Here, after Zengen first notified the Bank of the relevant facts, Zengen and Bank officials worked together both to figure out what had happened (Yen had absconded with Zengen's financial records) and to make sure it did not happen again. But just informing a bank of the relevant facts does

not necessarily inform it that it may become a defendant in civil litigation. The California Code requires this additional notification within a year.

Zengen argues that "businesspeople like those employed by Zengen are businesspeople, not lawyers, and especially not lawyers educated in the esoteric principles of the law of funds transfers," and they cannot be expected to know that the bank is liable for the loss. It also argues that a customer might not know "for an extended period of time" that it has a basis for a claim against the bank. The statute, however, does not require precipitate action. It gives the customer only a maximum of 90 days to notify the bank of the relevant facts in order to receive interest, but it allows a full year to object to the payment. One year is a substantial period of time. Indeed, it is the statutory time limit within which to commence some actions including, for example, an action "by a depositor against a bank for the payment of a forged or raised check, or a check that bears a forged or unauthorized endorsement . . . ." (Code Civ. Proc., § 340, subd. (c).) California Uniform Commercial Code section 11505 is not a statute of limitation but merely a statute of repose. (See Code Com., reprinted at 23D West's Ann. Cal. U. Com. Code, *supra*, foll. § 11505, p. 110.) It requires the customer only to notify the bank of the claim, not actually to commence the action. It is reasonable to require the customer to discover potential liability and notify the bank of a claim within a year of receiving notice of the payment.

This interpretation of section 11505's notice requirement is consistent with the Uniform Commercial Code's drafters' concern that "parties to funds transfers need to be able to predict risk with certainty, to insure against risk, to adjust operational and security procedures, and to price funds transfer services appropriately." (Code Com., reprinted at 23D West's Ann. Cal. U. Com. Code, *supra*, foll. § 11102, p. 27.) Reasonably prompt notification of a claim against the bank is important so the bank can investigate the matter, prepare a defense,

anticipate possible liability, and take steps to guard against similar future liability. Here, for example, the main factual basis for Zengen's claim for a refund is that the Bank did not follow the agreed security procedure of obtaining *verbal* authorization from Liu. Such a claim is best investigated reasonably promptly while memories are fresh.

Zengen also argues that section 11202, subdivision (b), requires the bank to prove an affirmative defense in order to avoid having to refund a payment of an unauthorized payment order. It argues that, because of this, a bank is always liable for accepting an unauthorized payment order unless it proves otherwise and, thus, informing the bank of the unauthorized payment order is tantamount to informing it that it is liable for the loss. We need not decide the exact meaning of section 11202 in this regard for it does not matter in interpreting section 11505. The fact remains that under the California Uniform Commercial Code a bank may or may not be liable for the payment depending on the circumstances. Section 11505 requires notice in some form that the bank may be liable for the loss; what procedure applies to deciding whether the bank is, indeed, liable is irrelevant to what the notice must contain.

Section 11505's notice requirement is not technical. The purpose of the notification requirement is to inform the bank reasonably promptly that the customer believes it is liable for the loss. That way, the bank knows it should take appropriate steps to protect itself. The customer's notice need only be sufficient to satisfy this purpose. The customer does not have to state specifically that it objects to the debiting or otherwise use any particular words. While it would certainly be preferable and clearer, and might avoid unnecessary litigation, for the customer to tell the bank expressly that the bank erred in processing the payment orders, or that it is liable for the loss, or use some other clear language, such specific words are not always necessary. What is necessary is that the customer

convey to the bank in some way that it objects to what the bank did or, stated slightly differently, it must in some way assert a claim against the bank. Whether the notification is sufficient in a given case depends on the overall circumstances.

We think the test should be whether, under all of the relevant circumstances, a reasonable bank would understand from the customer's communication that the customer was objecting to what the bank had done in accepting the payment orders or otherwise considered the bank liable for the loss. If a reasonable bank would so understand the communication, it would know it should take appropriate steps to protect itself, thus satisfying the purpose behind section 11505.

In this case, Zengen arguably did more than just inform the Bank the payment orders were unauthorized. Liu testified that he told Julie Yen *he* had not authorized the transactions, testimony that might be significant in light of the provisions of the funds transfer authorization agreement. Additionally, Liu testified that, at some uncertain time, he and Julie Yen had engaged in a "very general discussion . . . about bank being sued." The Court of Appeal did not decide the adequacy of Zengen's notification in light of the test we have expressed, and the parties have not briefed the question. We think it best to allow the Court of Appeal to apply the test in the first instance. (See *People v. Cahill* (1993) 5 Cal.4th 478, 510.) Accordingly, we will reverse its judgment and remand the matter to give it the opportunity to do so.

III. CONCLUSION

We reverse the judgment of the Court of Appeal and remand the matter to that court for further proceedings consistent with this opinion.

CHIN, J.

WE CONCUR:

GEORGE, C.J.
KENNARD, J.
BAXTER, J.
WERDEGAR, J.
MORENO, J.
CORRIGAN, J.

See next page for addresses and telephone numbers for counsel who argued in Supreme Court.

Name of Opinion Zengen, Inc. v. Comerica Bank

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Original Proceeding
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Judge: Teresa Sanchez-Gordon

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Pending California legislation of interest to bankers, as of July 7, 2007

AB 7 (Lieu, Saldans), as amended in Senate June 28, 2007. *Passed Assembly* (74-0), April 26, 2007. With Senate Appropriations. Hearing scheduled July 16, 2007. *CBA: Neutral*

Would add Financial Code 22345 and 23038 to make it unlawful – as of passage and signing by the Governor – under the California Finance Lenders law and the California Deferred Deposit Transaction Law to violate certain provisions of the John Warner National Defense Deposit Authorization Act for Fiscal Year 2007 (on payday loans to armed forces personnel). Would also exempt from the California law prohibitions against discrimination in lending against armed forces personnel, any person who does not market or extend consumer loans to armed services members and any person who does not market deferred deposit transactions to, or enter into such transactions with, armed services members. Bill would not apply to banks.

AB 14 (Laird), as amended in Senate, July 3, 2007. *Passed Assembly* (46-29), May 21, 2007. With Senate Appropriations, after do-pass (3-2) by Senate Judiciary, June 27, 2007. Hearing scheduled July 9, 2007. *CBA: Neutral if amended*

Civil Rights Act of 2007. Would, among many other things, amend the Song-Beverly Credit Card Act of 1971 to conform it to the Unruh Civil Rights Act, thereby adding disability, medical condition, marital status, and sexual orientation to the bases of prohibited credit card discrimination.

AB 18 (Blakesleee), as amended in Senate July 2, 2007. *Passed Assembly* (79-0), June 4, 2007. To Senate Judiciary. Hearing scheduled July 10, 2007. *CBA: Neutral as amended*

Warren Mattingly Signature Stamp Act.

Would only amend Elections Code 354.5 in other codes, on signature stamps made by persons who because of physical disabilities cannot write. Amendment would only apply for Election Code purposes.

AB 70 (Jones), as amended June 4, 2007. *Passed Assembly*, June 6, 2007. With Senate Judiciary (do-pass, 5-2, June 26, 2007). Hearing scheduled July 10, 2007. *CBA: No position*

Would add Water Code 8460 et al to provide that a city or county may be required to contribute its fair and reasonable share of the property damage caused by a flood, to the extent that the city or county increased the state's exposure by unreasonably approving new development in a previously undeveloped area, if the city or county failed to comply with existing law.

Other pending bills on water or flood control or disaster relief include:

> **AB 5** (Wolk), as amended in Senate, June 21, 2007. *Passed Assembly* (45-32), June 7, 2007. With Senate Judiciary. Hearing scheduled July 10, 2007

AB 62 (Nava), as amended in Senate, July 3, 2007. *Passed Assembly* (74-0), May 17, 2007. With Senate Revenue & Taxation. Hearing scheduled July 11, 2007

AB 156 (Laird), as amended June 1, 2007. *Passed Assembly* (78-1), June 5, 2007. With Senate Natural Resources & Water. Hearings scheduled July 10, 2007. *CBA: Support priority 3*

SB 05 (Machado), as amended April 25, 2007. *Passed Senate* (27-9), June 6, 2007. With Assembly Appropriations after do-pass by Assembly L.Gov. (5-1), July 3, 2007**.** *CBA: Support priority 3*

SB 17 (Florez), as amended June 4, 2006. *Passed Senate* (25-11), June 7, 2007. With Assembly Appropriations after do-pass (7-5) by Assembly Water, Parks & Wildlife, July 5, 2007

SB 34 (Torlakson), as amended April 17, 2007. *Passed Senate* (21-16), May 21, 2007. With Assembly Appropriations after do-pass (7-5) by Assembly Water, Parks, & Wildlife, June 26, 2007. Hearing scheduled July 11, 2007

AB 150 (Lieu), as amended June 1, 2007, 2007. *Passed Assembly* (71-8), June 5, 2007. With Senate Education after do-pass by Senate Water, Parks & Wildlife, June 26, 2007. Hearing scheduled July 12, 2007. *CBA: Support priority 3*

Would add Education Code 52980 et seq., the California Financial Literacy Initiative.

AB 512 (Lieber, Cote), as amended in Senate, July 5, 2007. *Passed Assembly* (47-29), June 7, 2007. With Senate Banking, Finance & Insurance. Hearing scheduled July 10, 2007. *CBA: Oppose*

Would amend Civil Code 1632 to extend California's "foreign language translation" statute to residential mortgages. Lenders would be required to provide a translation of the summary sheet of loan terms in the language in which the loan was negotiated, if that was either Spanish, Tagalog, Mandarin Chinese, Vietnamese, or Korean. A bank, etc., that makes loans secured by real property shall provide a summary translation of specified contract terms in each of those languages, as drafted by the Secretary of the Department of Business, Transportation and Housing.

AB 779 (Jones), as amended in Senate July 3, 2007. *Passed Assembly* (58-2), June 6, 2007. With Senate Appropriations after do-pass (3-2) by Senate Judiciary, June 26, 2007. Hearing scheduled July 16, 2007. *CBA: Oppose priority 2*

Would add Civil Code 1724 and amend Civil Code 1798.29 and 1798.82 to, among other things, make any retailer that violates the no-storage provisions of network rules liable to any card issuer harmed thereby.

AB 1168 (Jones), as amended in Senate July 2, 2007. *Passed Assembly* (75-0), June 6, 2007.

With Senate Judiciary. Hearing scheduled July 12, 2007. *CBA: Oppose priority 2 unless amended*

Would add Civil Code 1798.88 and 1798.89 and various other codes to, among other things, require that certain agencies redact social security numbers from certain records before publicly displaying such records. Also, no one could record or file with a local public agency any document that displays more than the last four digits of a social security number, unless required by state or federal law.

AB 1229 (Carter), as amended in Senate July 2, 2007. *Passed Assembly* (75-0), May 17, 2007. With Senate Public Safety. Hearing scheduled June 19, 2007, cancelled at request of author.

As introduced, would have added Penal Code 466.4 to make it a misdemeanor to possess an ATM card trapping device. As amended, now deals with membership on the Commission on Peace Officer Training and Standards. Will not be included in future listings.

SB 11 (Migden), as amended in Assembly, July 5, 2007. *Passed Senate* (23-15), June 4, 2007. With Assembly Appropriations, after do-pass (7-3) by Assembly Judiciary, June 25, 2007

Would amend Family Code 297 and 298.5 and Probate Code 2854 to eliminate the requirement that domestic partnerships be same sex.

SB 30 (Simitian), as amended in Assembly, June 12, 2007. *Passed Senate* (33-3), May 24, 2007. With Assembly Appropriations after do-pass (6-2) by Assembly Judiciary, June 19, 2007. Hearing scheduled July 11, 2007. *CBA: Oppose priority 3.*

Identity Identification Protection Act of 2007

SB 48 (Perata), as amended in Assembly, June 25, 2007. *Passed Senate* (23-16), June 7, 2007. With Assembly Appropriations after do-pass (12-4) by Assembly Health. July 3, 2007

Health care coverage

SB 385 (Machado), as amended in Assembly June 21, 2007. *Passed Senate* (34-1), June 6, 2007. With Assembly Business & Professions after do-pass (9-0) by Senate Banking & Finance, July 5, 2007. *CBA: Support priority 2*

Would amend Business Professions Code 101.31.1 and 10245 and add B&PC 10240.3, Financial Code 215.5, 22171, and 50333, and Government Code 13984 to require state-licensed mortgage lenders and brokers, banks, and credit unions to comply with the (federal) Interagency Guidance on Nontraditional Mortgage Product Risks and with the guidance on nontraditional mortgage products issued by the Conference of State Bank Supervisors and the American Associat0ion of Residential Mortgage Regulators. Wilful violations by real estate brokers or residential mortgage lenders would be a crime.

Bill would also expand the definition of real estate broker to include a person who engages as a principal in the business of making loans, with "in the business" defined as the making of eight or more specified loans to the public from the person's own funds.

SB 388 (Corbett), as amended in Assembly July 3, 2007. *Passed Senate* (22-17), May 31, 2007. With Assembly Judiciary. To third reading, July 5, 2007. *CBA: Oppose priority 2*

Would add Civil Code 60 et seq on radio frequency identification (RFID) tags. Any private entity that sells or issues a card with an RFID tag that is capable of being scanned for the cardholder's personally identifiable information must give certain information to the recipient. A recipient cardholder who is not so informed can sue any private entity that intentionally violates the law for $1,000 or actual damages. Attorneys fees and costs to the prevailing party.

SB 573 (Scott), as amended in Assembly July 2, 2007. *Passed Senate* (36-2), May 21, 2007. With Assembly Insurance. Ordered that bill be retained in committee, and subject matter be referred to Committee on Rules for assignment to the proper committee for study, July 5, 2007.

Would require any life insurance agent or insurer that pitches as annuity to a senior consumer have reasonable grounds for believing that the annuity is suitable for that consumer.

SB 1037 (Committee on Banking….), as amended April 23, 2007. *Passed Senate* (38-0), May 7, 2007. *Passed Assembly* (80-10), July 3, 2007. To enrollment. *CBA: Neutral as amended*

Would amend Financial Code 350, 697, 708, 1450, 1501.2, 1521, and 1522, and add Fin.C. 691.1 on corporate securities activities of banks, and exempting certain trust businesses from meeting certain requirements.

Bills that are likely dead, at least for this year

AB 26 (Nakanishi), as amended May 2, 2007. With Assembly Appropriations. Held under submission, May 31, 2007

Flood control

AB 36 (Niello), as introduced December 4, 2006. To Assembly Public Employees, Retirement & Social Security. *CBA: Neutral*

Would add Education Code 221010 and Government Code 20085 et seq. and 31455.5 to criminalize the making of false material statements re public employee retiree benefits or applications, or to knowingly accept public employee retiree benefits while knowing he/she is not entitled thereto. Jail, fines, and restitution.

AB 41 (La Malfa), as amended April 9, 2007. With Assembly Natural Resources.

Water resources: bond proceeds

AB 71 (Dymally), as amended April 9, 2006. With Assembly Revenue & Taxation. Hearing for testimony only, May 21, 2007.

As introduced, would have indexed the minimum wage to inflation. As amended, would allow a tax credit to small employers of a part of any amount paid for health insurance. Will not be included in future listings.

AB 75 (Blakeslee), as introduced December 4, 2006.

Spot bill on health care coverage for all working Californians and their families.

AB 78 (Torrico), as amended April 10, 2007. With Assembly Appropriations. Held under submission, May 31, 2007. *CBA: Neutral as amended*

Would amend and add various provisions of the Government Code to require that any committee regulated by the Political Reform Act of 1970 establish an account to include all contributions to a candidate, etc., with interest paid to the State Treasury, to be used by the Fair Political Practices Commission to enforce the Political Reform Act. A candidate-controlled committee could opt out of this requirement by paying the FPPC $ 5,000.

AB 245 (DeVore), as introduced February 1, 2007. With Assembly Revenue & Taxation. Held under submission, May 28, 2007. . *CBA: Neutral*

Would add and amend various provisions to the Revenue and Taxation Code to allow deductions for health savings account in conformity with federal law.

AB 267 (Calderon), as amended March 29, 2007. With Assembly Insurance. Hearing scheduled April 11, 2007, cancelled at request of author. *CBA: Support priority 3*

Would add Insurance Code 784.50 et seq. to require any insurance producer agent or insurer who pitches an annuity to a senior (age 65 or older) consumer to have reasonable grounds for believing that the annuity is suitable for that consumer.

AB 703 (Ruskin), as introduced February 22, 2007. With Assembly Judiciary. Hearing scheduled April 17, 2007, cancelled at request of author. *CBA: Neutral as amended*

Would add Civil Code 1798.555 to prohibit using a social security number as an identifier except when required by federal law. Any records with such numbers must be either encrypted or stored under lock and key, and when destroyed, done so through cross-cut shredding or some other manner that protects confidentiality.

AB 1301 (Gaines), as introduced February 23, 2007. With Assembly Banking & Finance. Hearing cancelled at request of author, April 24, 2007

Would repeal Financial Code 753 and amend Fin.C. 3516, to require Commissioner approval before any bank could deposit any of its funds with another corporation.

AB 1313 (Calderon), as amended April 24, 2007. With Assembly Judiciary. Hearing scheduled May 8, 2007, cancelled at request of author. *CBA: Support priority 3*

Would amend Civil Code 1747.85 to allow a card issuer to terminate all or substantially all of a class of the issuer's private label credit card accounts on 60 days after-the-fact notice, instead of 30 days prior notice.

AB 1418 (Arambula), as amended April 24, 2007. With Assembly Banking & Finance. *CBA: Support*

Would add Financial Code 14835 to require the Credit Union Advisory Committee (part of the Department of Financial Institutions) to develop a Credit Union Membership Investment Model that would identify credit union best practices in the areas of community development, small business and microenterprise financing, and investments of credit union capital. The model would have to be developed by July 1, 2009 and would be posted on the DFI's website.

SB 06 (Oropeza), as amended April 11, 2007. With Senate Local Government. Hearing postponed by committee, April 24, 2007

Land use planning; flood control

SB 31 (Simitian), as amended April 17, 2007. Held in committee without recommendation, April 24, 2007. To Assembly. *CBA: Neutral*

Would add Civil Code 1798.79 et al to make it a misdemeanor to remotely read (or attempt to remotely read) a person's ID.

SB 59 (Cogdill), as introduced January 11, 2007. With Senate Natural Resources. Failed passage in committee (3-4), April 24, 2007, reconsideration granted

SB 129 (Kuehl), as amended March 15, 2007. With Senate Public Safety. Held in committee without recommendation, March 27, 2007. *CBA: Oppose priority 3 unless amended*

Would amend Penal Code 653m to increase the penalties for intentionally annoying telephone calls, etc., if the call is in violation of a protective order, if the caller and callee have a specified relationship, or if a person knowingly permits a telephone, etc., under the person's control to be used for a prohibited purpose.

SB 270 (McClintock), as introduced February 15, 2007. With Senate Judiciary. *CBA: Support priority 3*

Would amend Code of Civil Procedure 1513 through 1521 on unclaimed property. Among other things, abandoned property held by a bank would escheat after 7 years instead of 3 years. Also, banks would have to send notices to apparent owners of safe deposit boxes concerning escheat.

SB 294 (Ackerman), as introduced February 15, 2007. With Senate Judiciary. Hearing scheduled March 27, 2007, cancelled at request of author.

Would amend Corporations Code 1502, 1502.1, 2117, and 2117.1 to excuse a publicly traded corporation from having to file certain reports with the Secretary of State if the corporation has a central index key that enables anyone to obtain information about that corporation from the SEC.

SB 461 (Ashburn), as introduced February 21, 2007. To Senate Public Employment and Retirement. Failed passage in committee (1-2), April 16, 2007. Reconsideration granted. *CBA: Neutral if amended*

Would add Government Code 7513.4 and 16642.5 to prohibit the Public Employees' Retirement System and the California State Teachers' Retirement System from investing public employment retirement finds in any company with business operations in a foreign terrorist state.

SB 596 (Harman), as introduced February 22, 2007. To Senate Judiciary. First hearing cancelled at request of author. *CBA: Oppose priority 2*

Would add Business & Professions Code 22949 et seq. to require that any computerized payment system sold as new in California to include antisniffer protection. A sniffer is a program or device that monitors data traveling over a computer network.

SB 638 (Romero), as introduced February 22, 2007. With Senate Banking, Finance & Insurance. Hearing scheduled May 7, 2007, cancelled at request of author.. *CBA: Oppose priority 1 unless amended*

Would amend Financial Code 14800 to allow state-chartered credit unions to offer lifeline banking (i.e., to sell money orders and to cash checks and money orders and receive electronic finds transfers) for persons not in their field of membership.

SB 752 (Steinberg), as amended April 18, 2007. With Senate Revenue & Taxation. Hearing cancelled at request of author, April 19, 2007. *CBA: No position*

Would add Government Code 99100 and Revenue & Taxation Code 17140.1, the California Kids Investment and Development Savings (KIDS) Account Ac. Every child born in California on and after January 1, 2008, would get a $ 500 investment account with the State Treasury.

Bob Mulford, July 7, 2007